THE 2011 FTA CORPORATE TREASURY SURVEY

AUSTRALIA AND NEW ZEALAND

FTA
FINANCE & TREASURY ASSOCIATION

THE UNIVERSITY OF QUEENSLAND
AUSTRALIA

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EXECUTIVE SUMMARY

The importance that survey respondents have assigned to various treasury functions has changed significantly in this year's survey. Interest rate and foreign exchange risk management are now the second and third most important functions respectively, eclipsing operational risk management which is now fourth. Cash and liquidity management remains the most dominant function, as in all previous surveys. A number of aspects of liquidity and cash management have strengthened. There has been an increase in the proportion of companies with a liquidity policy, and the vast majority monitor actual versus forecasted cash flows.

As would be expected with the increased importance of foreign exchange and interest rate risk management, hedging of these risks has also increased. Swaps retain their dominance as the instrument of choice in hedging interest rate exposures, as in previous years. In hedging foreign exchange exposure, a decline in the use of forwards has been offset by an increase in the use of cross-currency swaps.

This survey has uncovered a theme of increased diligence in monitoring credit risk and liquidity levels. The majority of respondents now monitor credit risk on a real-time basis. Almost all respondents now have a minimum liquidity policy. There have also been significant changes in the composition of and policies towards debt. The majority of respondents now have a policy to diversify borrowing sources, and there has been a significant increase in the proportion of funding sourced offshore. There has been a substantial level of deleveraging.

We are pleased to note a significant increase in the level of board involvement in treasury policy and risk management. Board understanding of financial exposures is generally strong, and most organisations report interest rate and foreign exchange risk management to the board. There has also been an increase in both the proportion of companies with a treasury policy, and that measure treasury performance. Despite these positive findings, several negative trends have continued through this survey. Reporting of limit breaches and non-compliance with policy to the board appears to be relatively low. There has been no improvement in such reporting over previous years. There has also been a continued level of dissatisfaction with information received from business units. As in the previous survey, the main complaint concerns the inaccuracy of information provided.

Unlike the 2006 survey which saw increases in nearly all responsibilities undertaken by treasuries, the 2011 survey presented data with no discernible trend. While small increases were seen in some functions, present tax planning (-23.6%), non-treasury risk management (-11.4%) and equity raising (-11.3%) showed significant decreases. These irregularities may be attributed to the global financial crisis (GFC) and subsequent recovery causing treasuries to restructure and become more streamlined. With respect to staffing numbers within treasury, there was a substantial decrease in the proportion of one person treasuries relative to 2006 levels (-29%). Conversely, steady rises were present in staffing levels above one person operations, particularly in the 4-8 person bracket (17.4%). Whereas there was an increase in the number of treasurers who found it 'easy' to recruit staff (2011: 12.5%, 2006: 7%), there was also an increase in the number of treasurers who had found it 'difficult' to recruit (2011: 39.6%, 2006: 22%)

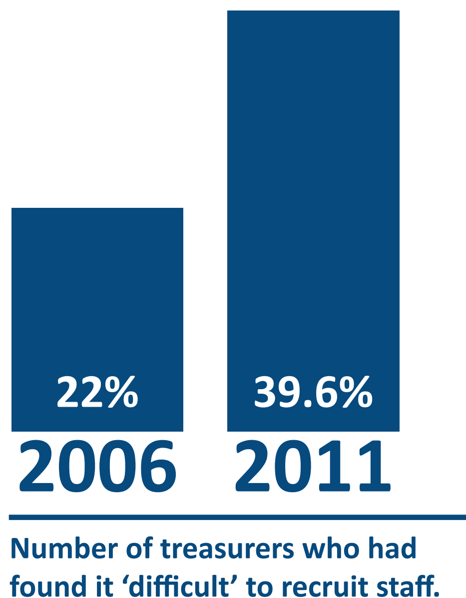
Questions regarding treasury systems in this year's survey indicated that 80.4% of respondents found they did not make full use of their Treasury Management System's (TMS) functionality (71% in 2006). There was also a rise in respondents who claimed the lack of using their TMS to its full potential stemmed from inadequate training/staff knowledge of system (2011: 35.5%, 2006: 13%). As technology continues to advance and software becomes more sophisticated, firms need to ensure that their staff are provided with thorough training when needed.

Australian and New Zealand companies have had much time since the 2006 survey to implement IFRS requirements. Over 60% of respondents reported no impact on their risk and a further 59% of respondents reported no impact on their ideal use of financial instruments. Most hedges used by respondents also qualified for hedge accounting under AASB 139/NZ IAS 39. Taken together, this would appear to suggest that most respondents were well prepared for the new standards.

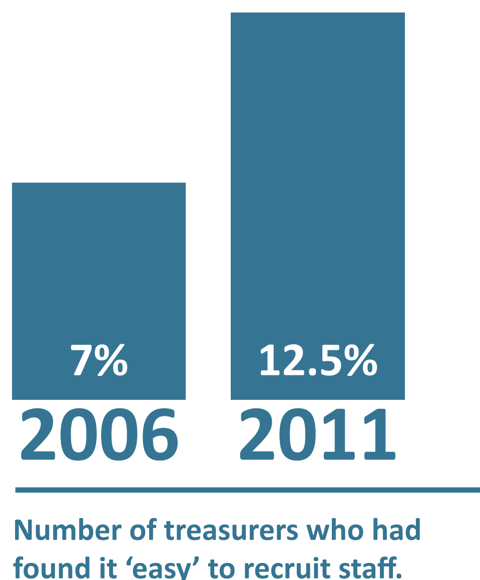
The survey revealed a significant increase in the use of Treasury Management Systems (from 18% to 82% of companies), primarily for core treasury functions, but also for derivative valuation and requirements associated with AASB 139/NZ IAS 39.

Treasurers were also asked to comment on what factors would drive change in the near future and what they would like to see improved in treasury operations. Reflecting the fallout from the global financial crisis, many respondents noted funding, liquidity and competitive pressures.

Respondents also noted the need for more investment in technology and better integration of treasury departments within organisations to respond to demands on most treasury departments to provide strategic risk management advice.



Number of treasurers who had found it 'difficult' to recruit staff.



Number of treasurers who had found it 'easy' to recruit staff.

KEY FINDINGS

FINANCIAL RISK MANAGEMENT

Foreign exchange and interest rate risk management have increased in prominence to become the second and third most important treasury functions in the 2011 survey. Cash and liquidity management remain the dominant risk management approach, as in previous years. Operational risk management has declined in importance relative to other functions.

Hedging of foreign exchange, interest rate and commodity price risk management have all increased markedly since 2006. The risk reward profile continues to be the most important factor in deciding which derivative instruments to use for hedging these risks.

Consistent with previous surveys, over 92% of respondents do not engage in speculative foreign exchange positions outside of normal hedging. Speculative interest rate positions are not utilised by any respondents.

All respondents who hedge interest rate risk use swaps, with an increase in the use of exotic options, exchange traded futures and options. There was a decline in the use of forward foreign exchange contracts, and an increase in the use of cross-currency swaps. Natural hedges remain the most popular method of hedging foreign exchange translation risk.

Although telephone trading remains the dominant method of transacting financial derivatives, the use of single bank proprietary dealing portals has increased significantly.

The regularity of credit risk monitoring has significantly increased since the global financial crisis, with the majority of respondents now monitoring on a real-time or daily basis. In measuring exposure to interest rate and foreign exchange fluctuations, sensitivity analysis has become the dominant method with value at risk analysis increasing in popularity.

LIQUIDITY AND FUNDING

The proportion of respondents with a liquidity policy has increased to 86% from 61% in 2006. Similar to previous surveys, 85% of respondents monitor actual versus forecasted cash flows. Of those who monitor, 66% reported a variance of less than 10% up from 60% in 2006. 10% reported a variance of greater than 20%.

Reflecting a general theme of increased diligence, 90% of respondents indicated they have a minimum liquidity policy, up from 58% in the previous survey. Allowance for short-term cash flow shortages was reported to be the most important factor in determining minimum liquidity reserve levels.

The majority of respondents indicated they had policies to diversify borrowing sources and stagger maturity dates of committed facilities. The weighted average maturity of debt is most commonly in either the one to three, or three to five year ranges. 26% of respondents indicated a weighted average maturity greater than five years.

There have been several major changes in the composition of domestic borrowing. The use of multi-option facilities has significantly declined since the last survey, while overdrafts and bank loans have increased, remaining the most used source.

An increased proportion of funds were sourced offshore, with the most popular markets continuing to be that of the US, Europe and Japan. The proportion of respondents reporting the use of a targeted gearing ratio has also increased since the last survey. Significant deleveraging was noted, with the most popular gearing band decreasing from 41 – 60% to 21 – 40%.

73% of respondents took steps to reduce working capital in the past two years. Of those who took these steps, over half reported they had tightened control over debtors.

GOVERNANCE, REPORTING AND CONTROL

Boards have become more actively involved in financial risk management and treasury policy decisions. Board involvement in setting, reviewing and approving treasury policies has increased markedly to 89% (2006: 73%). 41% of respondents also indicated the existence of a board risk committee.

70% of respondents indicated that their boards had either an excellent or strong understanding of financial exposures. The level of understanding was reported to be similar to that of executive management. Of those who felt improvement was required in this area, the most common recommendation was for increased treasury presentations.

More organisations are reporting interest rate and foreign exchange exposures to the board, continuing a theme of increased diligence in this area. While reporting of funding levels has maintained importance, reporting of cash balances declined. Only 55% of respondents report limit breaches and non-compliance with policy, a marginal improvement over the previous survey.

Respondents indicated a high level of dissatisfaction with information received from business units, most commonly regarding the inaccuracy of information. This marks the continuation of a trend identified in previous surveys.

The proportion of respondents with a treasury policy has increased to 95% (2006: 81%). The frequency of review of such policies has also increased, with 78% of respondents reviewing in the past year.

The survey shows a substantial increase in the proportion of respondents who measure treasury performance, reversing a decline seen in 2006. Of those who do measure, 78% were satisfied with their performance measures (2006: 82%). Of those who do not measure performance, 50% indicated the main reason was that it was not necessary for the nature and size of treasury activities.

TREASURY STRUCTURE AND STAFFING

The proportion of firms with a separate treasury unit has increased significantly compared to previous years. In 2011, 94% of responding firms have a separate treasury unit compared with 53% in 2006, 61% in 2004 and 70% in 2002.

Functions undertaken by treasury have seen irregular increases and decreases when compared with previous years. Cash and liquidity, and maintaining bank relationships continue to be the two main functions undertaken by treasury. The biggest increase (when compared with 2006 levels) has been in commodity price risk (up 9.4%) while the biggest falls have been seen in tax planning (down 23.6%), non-treasury credit risk (down 11.4%) and equity raising (down 11.3%). These results indicate that treasuries may be restructuring in response to the GFC and subsequent recovery.

There has been a dramatic decrease in the number of one-person treasuries compared to 2006 levels.

A small number of recruiters within treasury departments found it easier to recruit qualified staff in 2011 (12.5%) than in 2006 (7%) whereas 39.6% (2006: 22%) of recruiters found it more difficult to do so.

The profile of the treasurer continues to be predominantly male, aged between 41-50 years. The proportion of female treasurers has remained approximately constant (13.8%). The majority of staff in treasury expect to be undertaking the same role in five years' time. Treasurer remuneration has again increased with 46.5% of treasurers earning in excess of $250,000.

Outsourcing has decreased in 2011 with only 19.1% (2006: 28%) of respondents indicating that their treasury has outsourced or intends to do so.

Predictably, the main driver for this outsourcing has been cost efficiency.

KEY FINDINGS

TREASURY SYSTEMS

The main TMS and valuation systems used include Integra-T, Quantum and Visual Risk with each system accounting for approximately one fifth (19.6%) of total responses. 19.6% of respondents claimed their treasury did not have a main proprietary TMS and either did not plan on implementing one (10.7%) or was considering one in the next 2 years (8.9%). Core treasury functions (78%) used the TMS and valuation systems most extensively.

80.4% of respondents stated they did not make full use of their TMS and valuation system's functionality. The main reason for this was that users did not require all of the functions within the system.

ACCOUNTING AASB 139/NZ IAS 39

Respondents appeared to have transitioned to the IFRS well, with over 59% of respondents noting that there were no changes to the use of financial instruments.

Recognition and measurement of embedded derivatives has substantially improved, and most respondents are using Treasury Management Systems to assist in complying with IFRS requirements.

There has also been a large increase in the number of respondents using statistical techniques to test hedge effectiveness.

MAJOR ISSUES, DRIVERS OF CHANGE AND FUTURE DIRECTIONS

The Global Financial Crisis had a major impact on treasury operations in the recent past, and continues to drive changes in the Treasuries of respondents.

Also related the crisis are the increasing demands on treasury departments to provide strategic advice in relation to company balance sheets and risk management in general, in additional to compliance with an increasing regulatory burden.

Given the responsibilities, Treasurers highlighted the need for more investment in technology, provision of more resources and greater integration with other business units.

M+
6,750
6,500
6,250
6,000
80.4%
of respondents stated they did not make full use of their TMS and valuation system's functionality.

FINANCIAL RISK MANAGEMENT

RISK MANAGEMENT APPROACH

Management of operational risk has decreased in importance from being a key function for 47% of respondents in 2006 to 31% in 2011, and is now the fourth most important treasury function (previously second). As in previous surveys, the management of cash and liquidity is still regarded as the most important function, being identified by 96.7% of respondents (2006: 90%, 2004: 81%). The importance of foreign exchange and interest rate risk management has significantly increased to become the second and third most important functions respectively. Refer to Chart 1.

Hedging of both foreign exchange and interest rate risks remains strong at 85% and 71% respectively, an increase in both forms over 2006 levels. 43% of respondents indicated that they faced commodity price risk and the level of hedging of this risk increased to 75% compared with 40% in 2006.

The two main reasons stated by respondents for hedging are to achieve certainty of cash flows, margins, revenues and costs and to protect the value of assets and liabilities. These results are consistent with previous surveys.

The risk reward profile continues to be the most important factor in determining which instruments to use for hedging, having further increased in importance from the 2006 level. Price is the second most important factor.

Other factors considered important are:

- Accounting treatment;
- Ability to value and mark to market the transaction; and
- Market liquidity of the instrument.

Regarding speculative positions, over 92% of respondents did not allow speculative foreign exchange positions outside of normal hedging. No respondents allowed speculative interest rate positions.

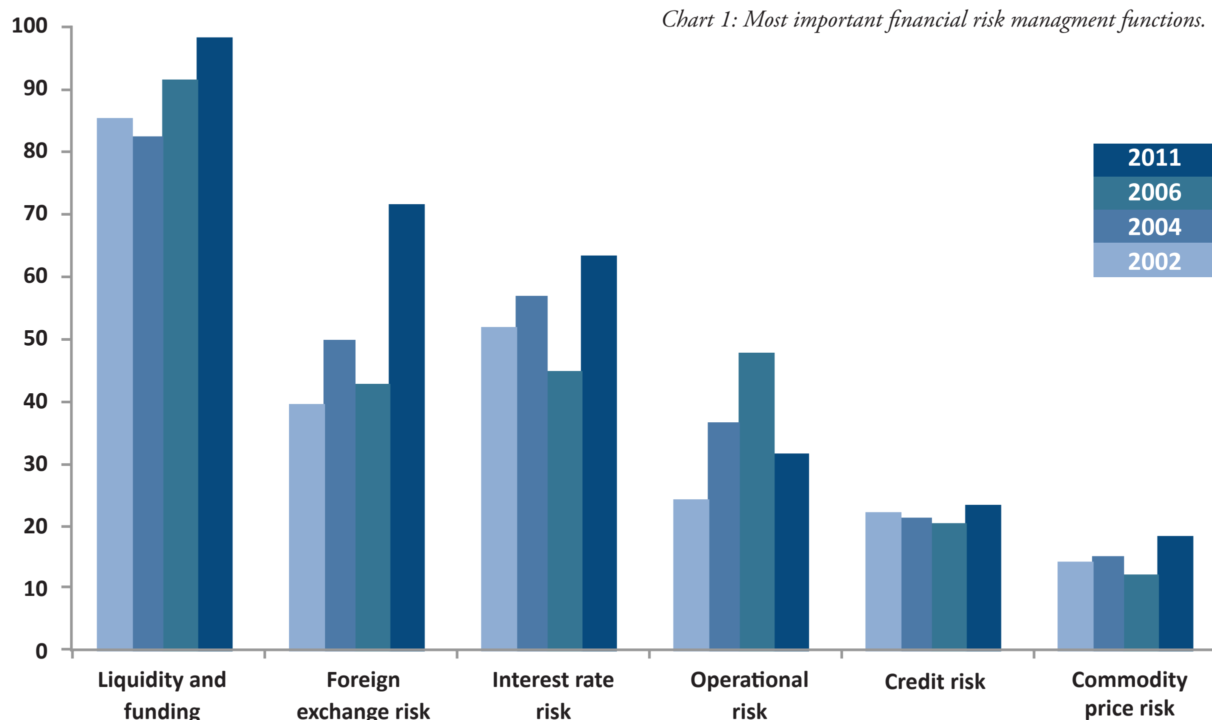


Chart 1: Most important financial risk managment functions.

INTEREST RATE RISK MANAGEMENT

Hedging practices have changed since the last survey, with 81% of respondents who hedge now doing so within a range (2006: 69%). Only 6% now hedge a fixed proportion (2006: 21%). The proportion of respondents who hedge all exposure has increased to 13% (2006: 10%). Only 13% of respondents use quantitative analysis to determine the hedging proportion, with the remainder relying on judgement of management and the board.

Respondents were asked what average time horizon they used for hedging interest rate exposure. 15% of respondents had no predetermined time horizon used for managing interest rate risk. Chart 2 shows the average time horizon for interest rate risk management.

The instruments used for interest rate risk management are shown in Chart 3. This Chart shows changing trends in the instruments used since 2006. All respondents now employ interest rate swaps, and there has been an increase in the usage of exotic options and exchange traded options and futures. Forward rate agreements have maintained similar importance, while the use of swaptions has declined slightly.

The increased use of interest rate swaps may reflect the strong interest rate differentials persisting across developed countries over the past few years. Prolonged recovery in Europe and North America in contrast to the surging growth in the Asia Pacific may have led to changing comparative borrowing advantages among respondents.

Chart 2: Time horizon for interest rate risk management

Chart 3: Interest rate instruments used

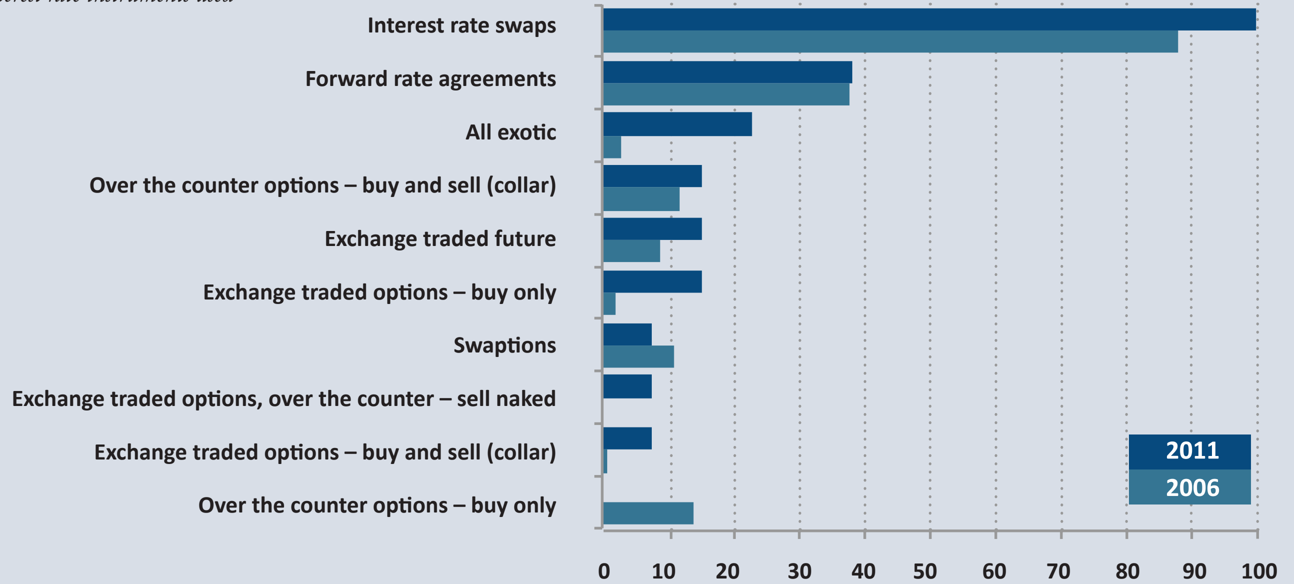


Chart 4: Time horizon for hedging foreign exchange

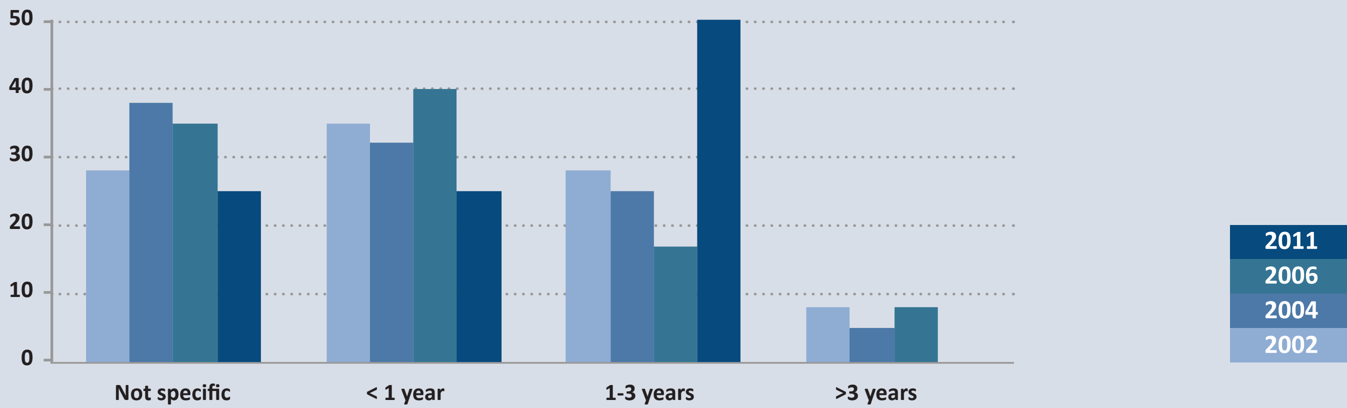
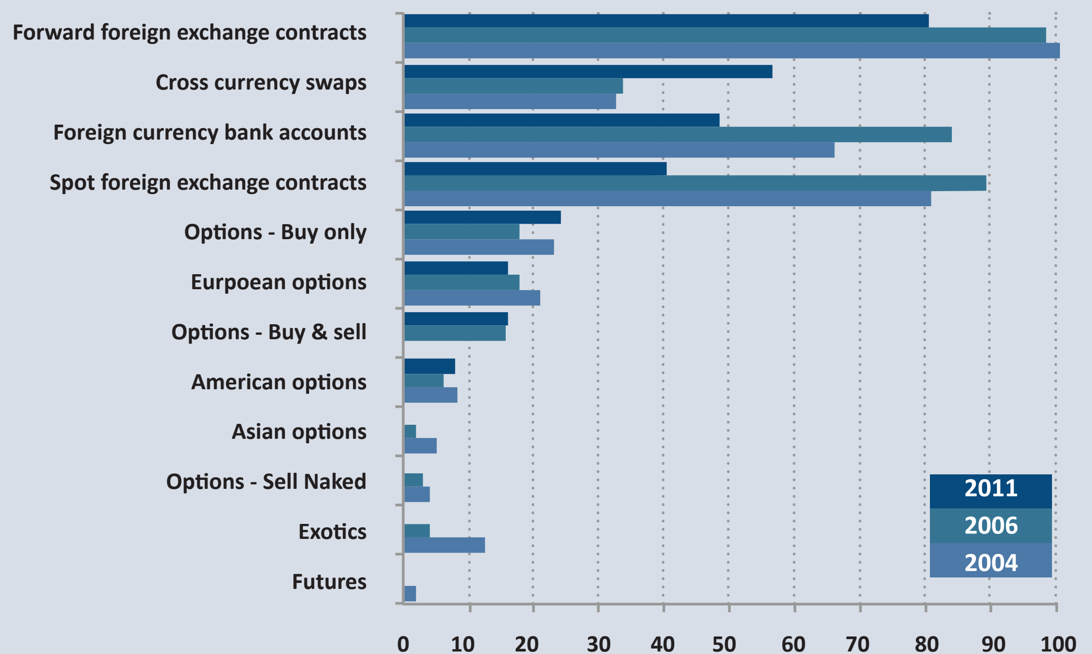


Chart 5: Foreign exchange instruments used



FOREIGN EXCHANGE RISK MANAGEMENT

Over 80% of respondents indicated exposure to foreign exchange risk. Of these:

- 15% do not hedge;
- None hedge a fixed amount (2006: 10%);
- Two thirds hedge a range (2006: 48%); and
- One third hedge all exposure (2006: 49%).

Additionally, 54.5% of respondents net offset foreign exchange transaction exposures. This has declined for the past three surveys.

Respondents were asked if they apply the same foreign exchange hedging policy to capital expenditure and operating expenditure. The vast majority (87.5%) indicated the same policy parameters applied, a significant increase over previous years (2006: 71%, 2004: 62%).

Chart 4 shows that the average time horizon used for hedging foreign exchange risk has significantly increased, with 50% of respondents indicating hedging in the 1-3 year range (2006: 17%)

Chart 5 shows the instruments used for foreign exchange risk management. There has been a marked shift in the major instruments used; with a significant decline in the use of forward foreign exchange contracts and an increase in cross currency swaps.

DEALING PORTALS

The 2011 survey reaffirms the dominance of phone trading, unchanged from the previous two surveys at 76%. However the popularity of single bank proprietary dealing portals has increased, now employed by 36% of respondents. Consistent with previous surveys, approximately half of all respondents expect to use bank portals in the next two years.

MANAGEMENT OF FOREIGN EXCHANGE TRANSLATION RISK

Respondents were asked if they have foreign exchange translation exposure arising from offshore assets, such as investment in offshore subsidiaries, or from liabilities, such as loans in foreign currencies. 85% of respondents indicated exposure from assets and revenues, however no respondents indicated exposure from foreign liabilities.

The use of natural hedges, such as offsetting foreign currency assets with liabilities and vice versa, was the most common method in managing this exposure. For respondents sourcing funds offshore to manage translation risk arising from foreign assets and revenue, the amount of funds to source remains a contentious issue.
The following factors were stated as being drivers for the amount of foreign debt to source:

- The preferred gearing ratio set for the asset (2011:44%, 2006: 30%);
- Thin capitalisation rules (2011:44%, 2006: 81%); and
- Comparative value of interest rates (2011:14%, 2006: 44%).

COMMODITY PRICE RISK MANAGEMENT

Respondents were asked if they were directly exposed to commodity prices, and if so, which commodities they were exposed to. 43% of respondents indicated exposure. Chart 6 shows the percentage of respondents exposed to various commodities.

The majority of respondents exposed to commodity price risk either hedge a fixed proportion or a range of their exposure. The most common time frames for hedging were up to one year, and up to three years. The proportion that hedge over three years has declined to zero from 10% in previous surveys.

The most popular instruments for hedging commodity price exposure are options, with respondents also indicating the use of swaps.

Respondents indicated that the main reason for hedging commodity price risk was to achieve certainty of cash flows, margins, revenues and costs. Attempts to maximise benefit from market fluctuations on the hedged item was also a consideration, and may explain the popularity of options in this context.

CREDIT RISK

Since the previous survey and subsequent Global Financial Crisis, there has been a significant change in the monitoring of credit risk. Of those who monitor credit risk, 22% now monitor on a real time basis (2006: 14%), 34% monitor on a daily basis (2006: 28%) and 44% monitor less frequently (2006: 59%). The percentage of respondents who have a counterparty credit risk policy is slightly higher at 89%, compared with 87% in 2006.

Respondents were asked how they manage credit risk. The results were somewhat different to prior years, in that the percentage of organisations using various risk management approaches increased in every category:

- 93.4% establish limits based on the credit rating of the counterparty (2006: 89%);
- 49.2% limit exposure to a particular amount for particular companies (2006: 42%);
- 23% establish country limits (2006: 7%); and
- 18% limit the number of transactions with any counterparty (2006: 3%).

The increased level of credit risk management are likely to be the result of higher risk aversion following the GFC . The methods employed for measuring credit exposure on derivative positions is shown in Chart 7.

RISK ANALYTICS

There has been a noticeable increase in the proportion of respondents engaging in exposure analysis in managing foreign exchange and interest rate risk management. The proportion of respondents engaging in commodity price risk exposure analysis remains largely unchanged since the 2006 survey. In managing foreign exchange and interest rate risk, sensitivity analysis appears to have become the dominant method. At risk analysis has also increased in popularity, particularly for the management of interest rate risk. The proportion of respondents undertaking analysis by exposure type is shown in Chart 8.

Of the respondents who undertake exposure analysis, 43% report the analysis to the board. The dominant reporting frequency is monthly.

Among respondents who don't use risk analytics, the most prevalent reasons were:

- Too complex for size of operations (44%);
- Insufficient resources to establish and maintain (42%); and
- Do not believe any value added (37%).

Chart 6: Exposure to commodities

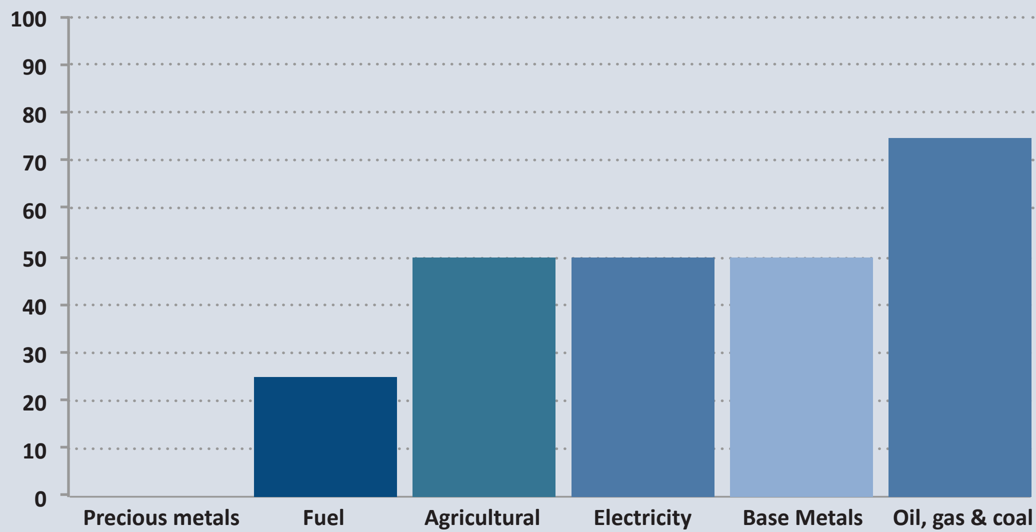


Chart 7: Calculation of credit exposure on derivative positions

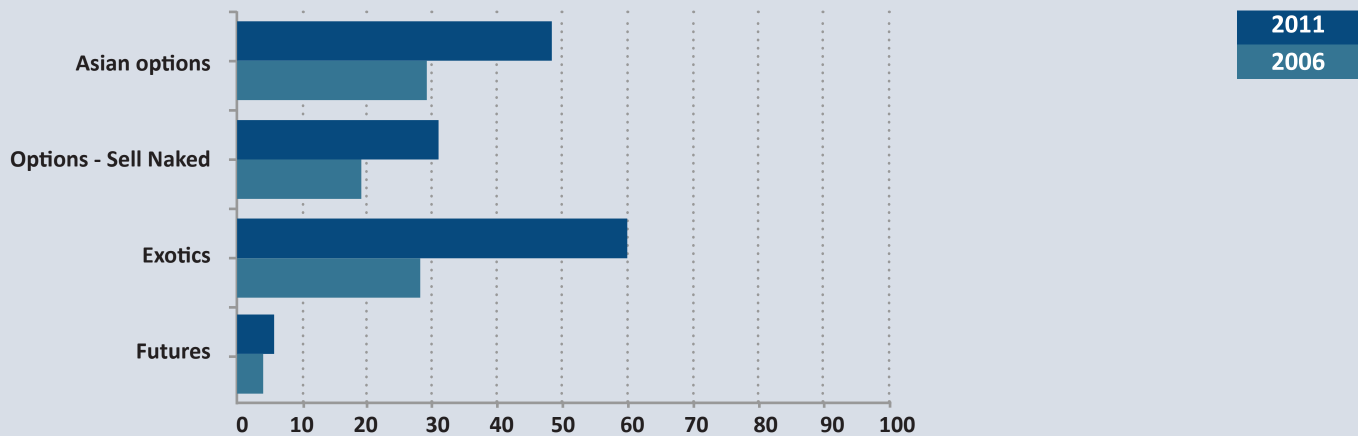
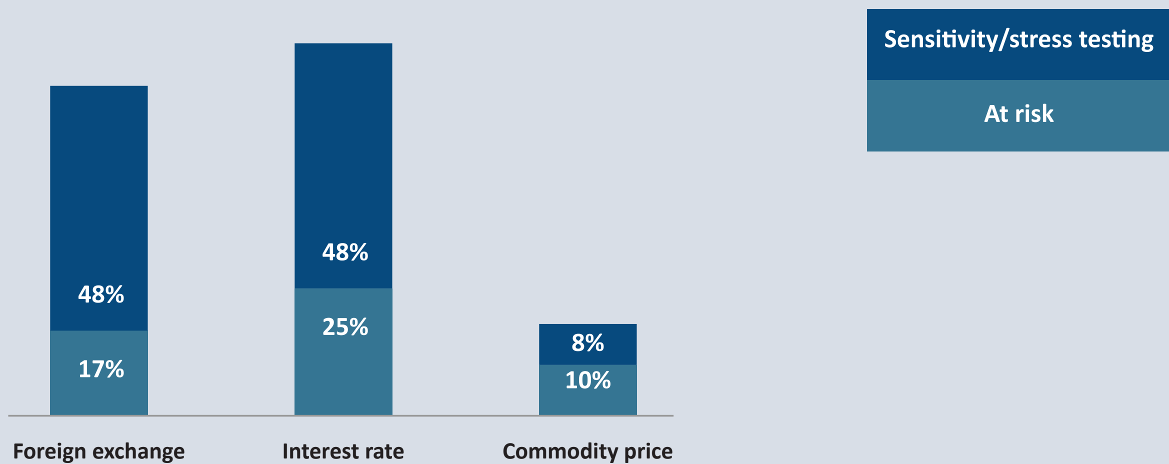


Chart 8: Undertaking of exposure analysis



LIQUIDITY AND FUNDING

FINANCIAL RISK MANAGEMENT

The proportion of respondents that have a liquidity policy has significantly increased since past surveys to 86% (2006: 61%, 2004: 70%).

As in previous years, the dominant method of sourcing cash flow data continues to be a combination of reports from financial support systems and advice from business units (57% of respondents). The use of other methods, such as integrated business wide systems and direct input by business units into treasury models, remains benign at less than 10%.

Time horizons over which respondents performed cash flow forecasting were similar to the results of previous surveys. 67% of respondents undertake daily forecasting, 61% monthly and 43.5% annually.

The vast majority of respondents monitored actual versus forecast cash flows (85%). A reduction in the average variance of actual versus forecast cash flows reported since 2006 is shown in Chart 9. The increased accuracy of cash flow forecasting may reflect greater diligence in the wake of the global financial crisis.

There has been a significant change in policies on minimum liquidity reserves since the 2006 survey, continuing the theme of heighted post-GFC risk aversion and diligence. 90% of respondents now have a policy on minimum liquidity reserves, compared with just 58% in 2006, and 56% in 2004.

Allowance for short-term cash flow interruptions has emerged as by far the most important factor in determining levels of liquidity reserves (Chart 10). Maintaining liquidity reserves as a buffer against economic downturn was also indicated to be a vital factor. Such heightened risk aversion may stem from the recent volatility of market conditions and sluggish growth rates in developed economies.

In determining the liquidity reserve level, the three most commonly cited methods were:

- An absolute value approved by the board / executives (61%);
- A percentage of forecast short-term net debt levels (21%); and
- Related to forecast of net receivables over a specified time period (17%).

Cash or liquid investments continue to be the most common form of liquidity reserve at 70% (2006: 68%). Other important forms included committed facilities and parent guarantees.

Chart 9: Actual to forecast -average variance

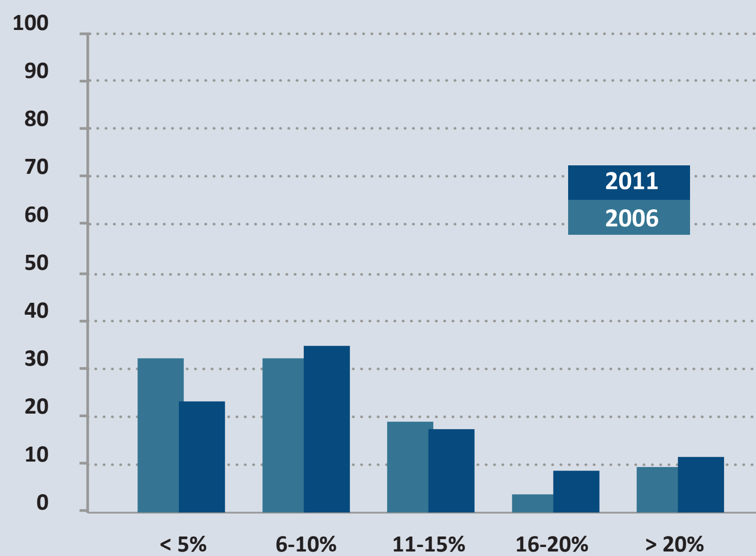
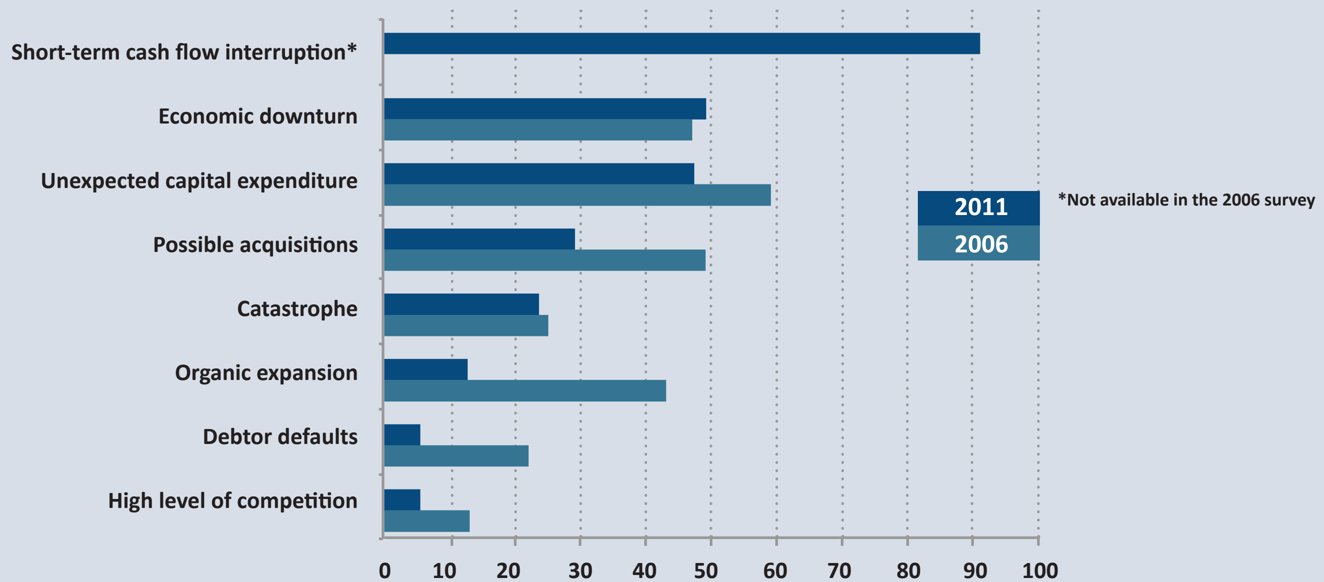


Chart 10: Factors determining levels of liquidity reserves



BORROWINGS

Reflecting changing metrics of corporate credit, the proportion of respondents that have a policy to diversify borrowing sources has increased to 62% (2006: 40%). Further to this, 74% of respondents indicated that they have a policy to stagger maturity dates of committed facilities (2006: 50%).

Survey results indicate a weighted average maturity of corporate debt that is most commonly either one to three years, or three to five years (one third of respondents in each category). 23% of respondents have a weighted average maturity of debt between 5 and 10 years, with just 2.6% exceeding 10 years.

Respondents were asked what factors were important in determining the length of maturity of debt. Consistent with previous surveys, liquidity needs were taken to be the most important factor at 71% (2006: 79%). Other important factors included asset life, balance sheet structure and interest rate forecasts. Refer to Chart 11.

Overdrafts and bank loans are the most popular domestic source of short-term funding, with bank loans increasing in popularity from 25% in 2006 to 67% in 2011. The use of multi option facilities has reversed an earlier increasing trend, falling significantly in popularity since the last survey (Chart 12).

Fixed and floating rate funding are now equally popular as long-term funding sources. 56% of respondents indicated they had sourced more than 25% of their organisation's total senior debt from the capital markets. 30% of respondents indicated they had raised more than 75% of their funding in this way.

Respondents were asked what proportion of debt they source domestically. Continuing a trend in previous surveys, there has been an increase in reliance on offshore funding. 54% of respondents indicated that they source more than half of their funding offshore. Refer Chart 13.

Among those respondents who sourced debt offshore, the US debt markets were most commonly relied upon (43%, 2006: 40%). Other notable markets included European (18%) and Japanese (14%).

Chart 14 shows the average credit margin achieved across the respondents' main facilities at both the current time, and their estimate of the margins 2 years ago. Only 28% of respondents a chieve a margin of 1% or less, compared with 58% 2 years ago. The proportion of respondents achieving sub LIBOR / BBSW has dropped, and the proportion unable to achieve a spread of less than 2% has increased markedly.

The proportion of respondents with a targeted gearing ratio has increased significantly since the previous survey, now at 63% (2006: 41%). The most favoured ratio band is now 21 – 40%, where it was 41 – 60% in 2006.

WORKING CAPITAL

73% of respondents indicated that they had undertaken initiatives to reduce working capital in the past 2 years. Of those respondents, 54% indicated that they had tightened control over debtors, while 39% indicated that they had reduced net cash flows. Only 27% of respondents indicated that business units and subsidiaries were charged a cost for working capital funds.

Chart 11: Factors determining length of debt

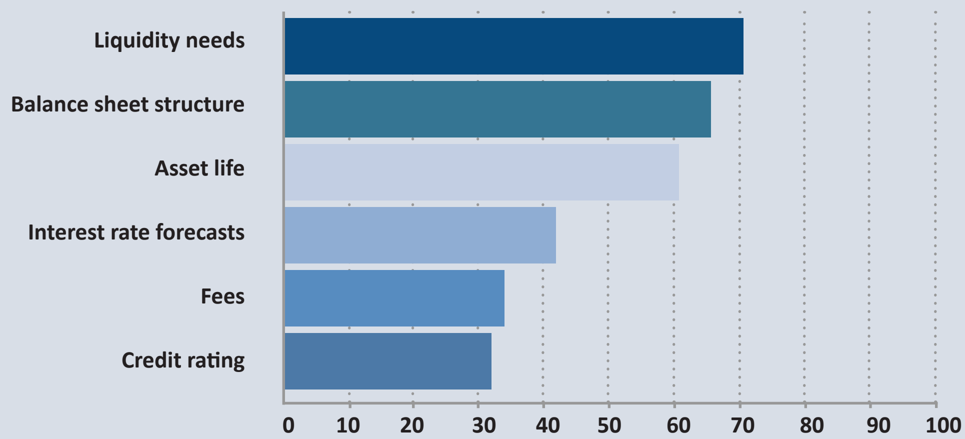


Chart 12: Domestic Borrowing Sources

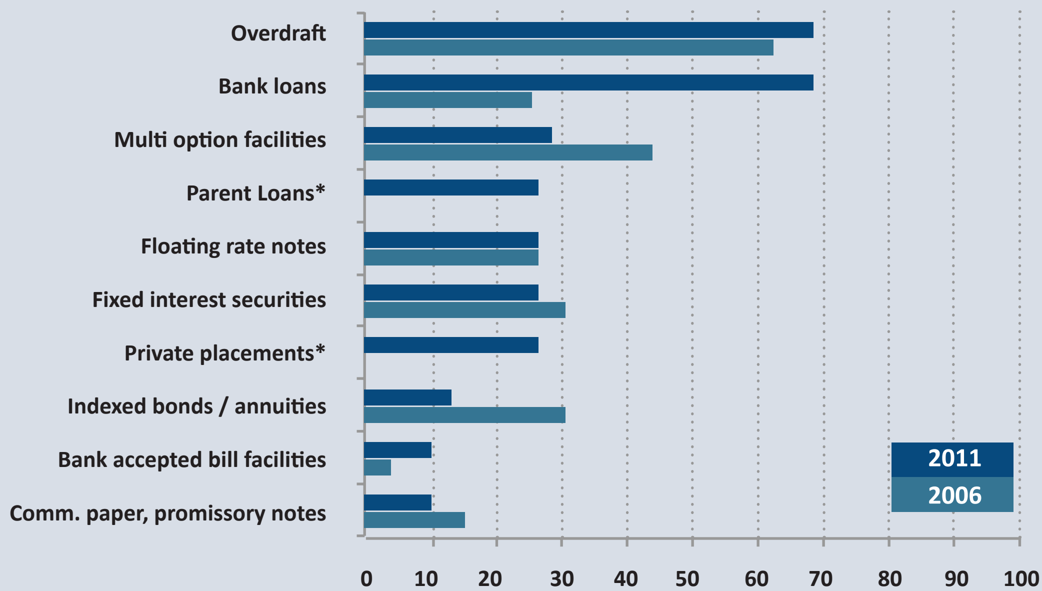


Chart13: Proportion of debt sourced

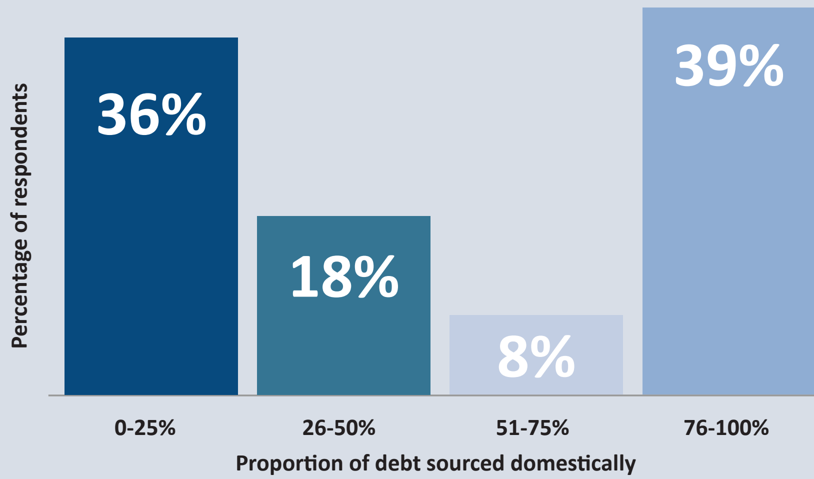
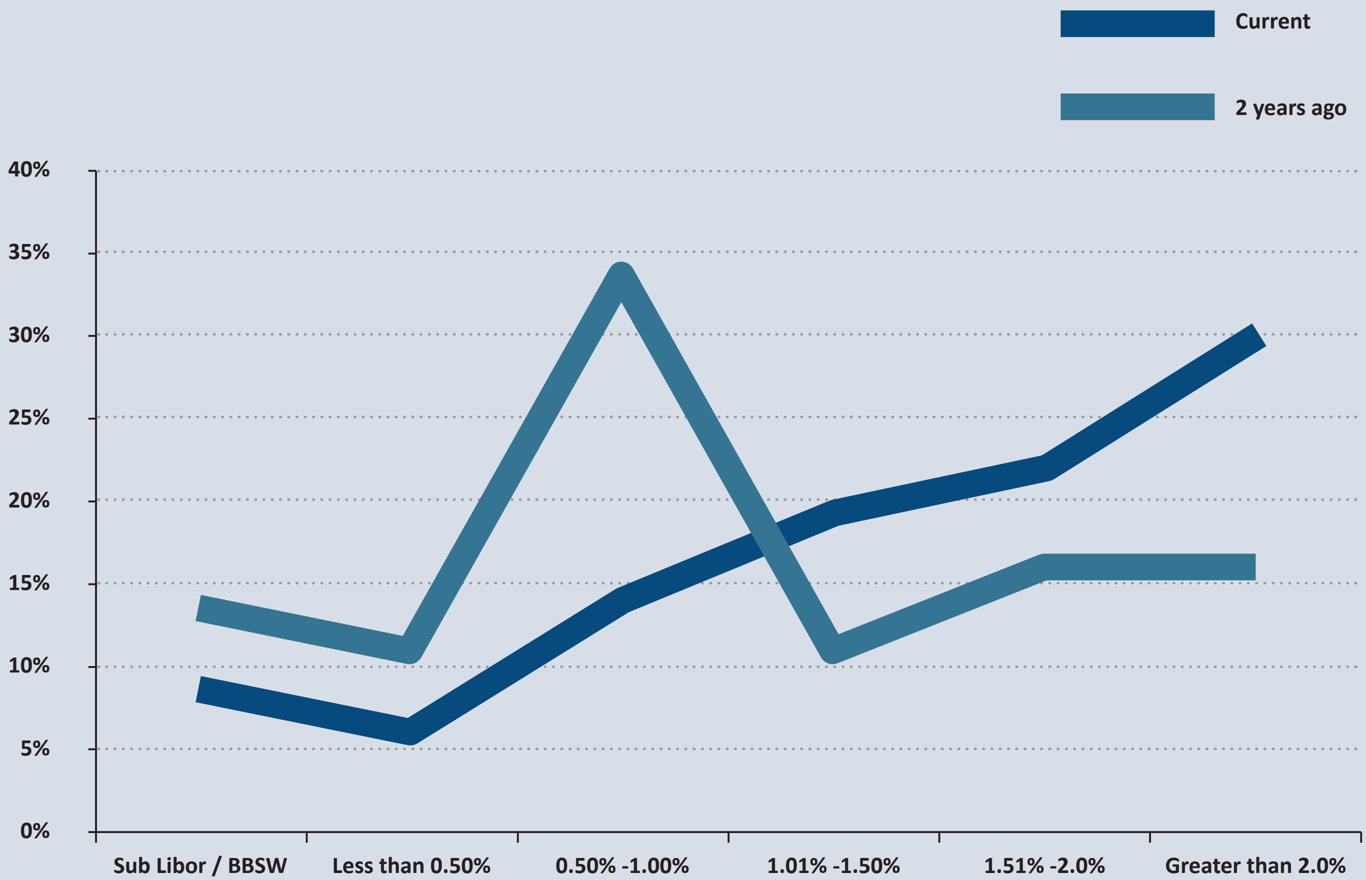


Chart 14: Average credit margin across main facilities



73%
of respondents indicated that they had undertaken initiatives to reduce working capital in the past 2 years.

GOVERNANCE, REPORTING & CONTROL

THE ROLE OF THE BOARD

Boards have become more actively involved in financial risk management, continuing the trend from previous years. Board involvement in setting, reviewing and approving treasury policies has increased markedly to 89% (2006: 73%). See Chart 15.
The provision of input into strategic financial risk management decisions has remained at 2006 levels. The lack of increase in this input may be explained by the designation of such decisions to board risk committees. 41% of respondents reported the existence of such a committee.

Respondents indicated that boards had a relatively strong understanding of financial exposures (interest rate, foreign exchange, liquidity, credit and commodity price risks), consistent with previous surveys. 19% of boards were rated as excellent, 51% good, and just 2% rated poor by respondents.

Of the respondents that felt improvement in their board's understanding was required, the most common recommendations were for treasury presentations to the board and training/professional development of directors.

BOARD REPORTING

Increased reporting of interest rate and foreign exchange exposures from treasury to the board since the last survey indicates that directors have increased their focus on financial exposures (Chart 16). This may reflect the increase in volatility of both the currency and interest rate markets during and in the wake of the GFC. Funding levels maintained their importance, increasing to 82% from 78% in 2006. Conversely, the importance of reporting cash balances to the board appears to have significantly declined to 70% (2006: 86%), and is now only the fourth most important reporting area.

The lack of reporting of limit breaches and non-compliance with policy was noted in previous surveys, and continues to be an area of concern. Although improving slightly, 45% of respondents still do not report limit breaches and non-compliance with policy.

Feedback received by treasury regarding information provided to the board appears to be less positive than previous surveys. Only 46% of respondents received no complaints, down from 77% in 2006 and 2004. The most common complaints received were that information was either not detailed enough or was too confusing. 76% of respondents indicated that treasury reported to the board on a monthly basis, with 21% reporting quarterly.

Chart 15: Board Involvement

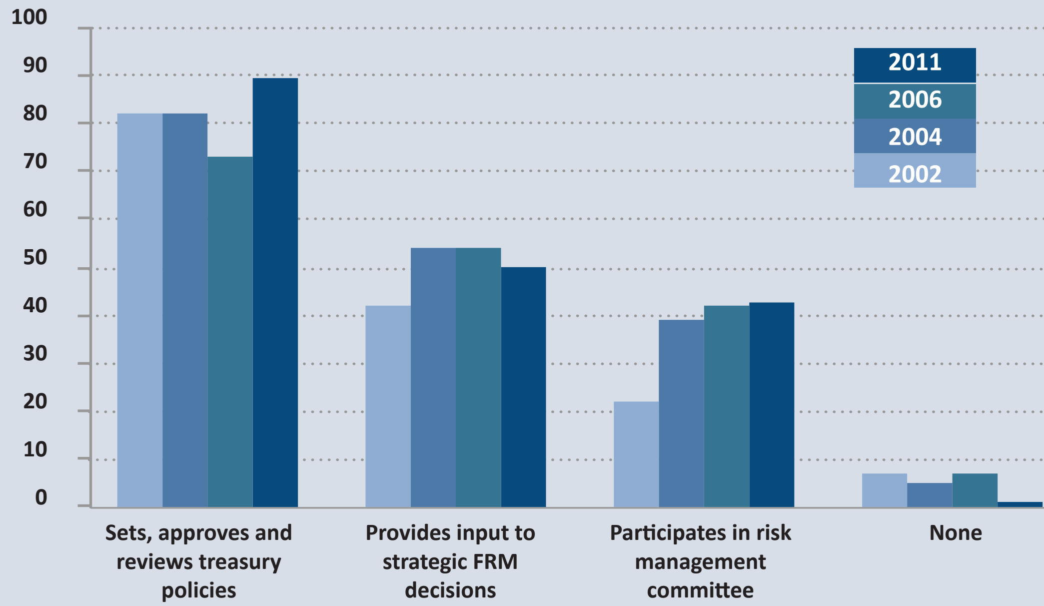


Chart 16: Board Reporting

Interest rate exposures
Funding (debt levels and maturity profiles)
Foreign exchange exposures
Cash balances
Forecast covenant ratios*
Treasury couterparty credit exposures
Positive assertion of policy compliance*
Non-compliance with policy
Breaches of limits
Market overview / commentary
Cash flow forecasts
Forecast debt facility utilisation
Forecast investment profile*
Commodity price exposures

2011
2006
2004

*Not available in the 2006 survey

0 10 20 30 40 50 60 70 80 90 100

INFORMATION FLOWS

- **Information provided to executive management.** Executive management's satisfaction with information provided by treasury is similar to that of the board. 45% of respondents received no complaints, while 49% received complementary remarks. As with the board, the most common complaint was that information was not detailed enough. Respondents indicated that executive management's understanding of financial exposures (interest rate, foreign exchange, liquidity, credit and commodity price risks) had increased, reversing a previous trend (78% rated as either excellent or good compared with 72% in 2006). As would be expected, executive management's understanding of these exposures exceeds the board's understanding (70% as either excellent or good for the board).
- **Information received from business units**. Respondents in past surveys have indicated a relatively high level of dissatisfaction with information received from business units. This trend has continued, with only 21.6% of respondents indicating treasury made no complaints, and 25% indicating that praise was given. Chart 17 shows that timeliness and accuracy of information are the most problematic areas.

CONTROL OF THE TREASURY FUNCTION

Almost all respondents (95%) indicated that they have a treasury policy, a substantial increase since 2006 (81%). This is most commonly in the form of a single document (61%), or a comprehensive series of individual policies covering all financial risk management activities (including front, middle and back offices). Further to these positive developments, the frequency of review of treasury policy has also significantly increased with 78% of respondents reviewing the policy in the past year (2006: 57%). This may represent further evidence of a shift in approach to risk management since the GFC. The most common inclusion in the treasury report was purpose and scope of the policy. See Chart 18. Consistent with the trend towards increased diligence in managing foreign exchange and interest rate risks, these exposures are among the most common components of treasury reports.

PROCEDURES MANUAL

81% of respondents have a treasury procedures manual. An alarming trend manifesting over previous surveys of an increasing number of organisations with no procedures manual appears to have reversed (In 2006, 37% of respondents had no procedures manual, compared with 19% this year). See Chart 19. 64.5% of respondents indicated that they had updated this manual in the past year, with 82.5% updating in the past two years. 6.3% have never updated their procedures manual.

SEGREGATION OF DUTIES

Respondents were asked how they segregate duties between treasury functions. 40% indicated that they separate into three areas: front office (dealing), middle office (management reporting and confirmations) and back office (settlement and accounts). Interestingly, 43% segregated front office while combining back and middle office. Just 8% did not segregate. See Chart 20.

TRANSACTION CONFIRMATIONS PROCESS

In confirming outgoing transactions (excluding the 11am money market), facsimile and email are the most popular mediums (53% and 45% respectively). Incoming confirmations were most commonly printed. Only 10% of respondents indicated that they utilised an automated, system-based matching process.

DOCUMENTATION AND SETTLEMENTS

There has been a significant increase in the proportion of respondents indicating they use International Swaps and Derivatives Association agreements in the 2011 survey. 99% of respondents to whom it was applicable reported use of the agreements (2006: 60%). Of these, 81% used them for all counterparties.

Chart 17: Business unit information

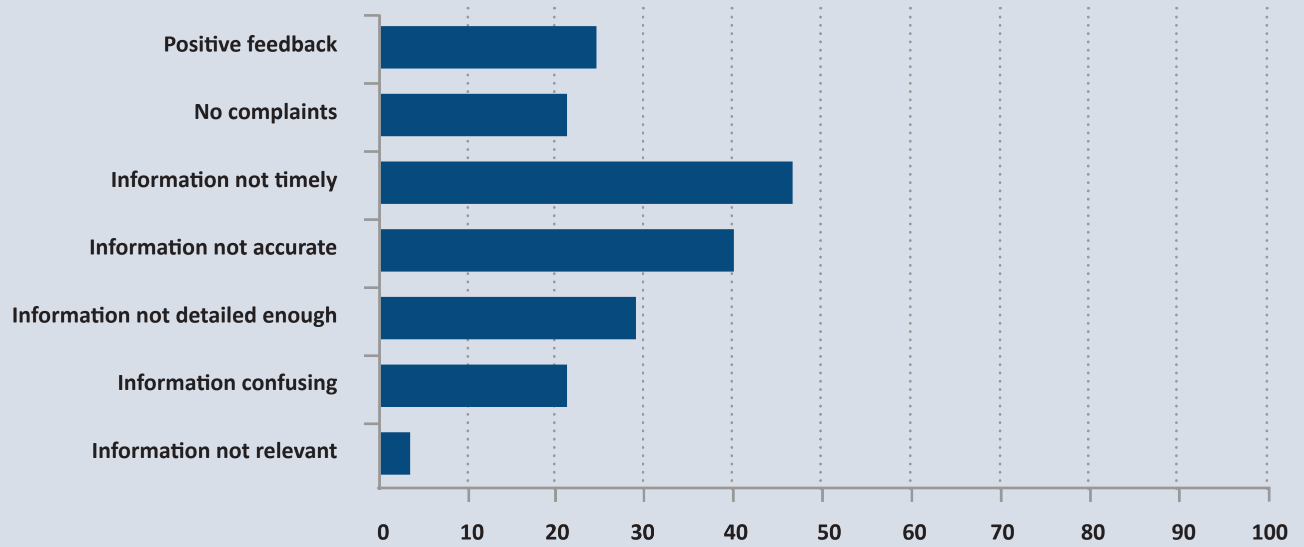


Chart 18: What is included in the treasury policy

Purpose and scope of the policy
Foreign exchange
Interest rates
Role of Treasury in managing financial risks
Liquidity & funding
FRM objectives
Counterparty credit risk
Authorised instruments and arrangements
Reporting to management and the Board
Credit limits
Delegation of authority
Derivatives policy
Organisational structure, responsibilities
Speculative trading reference
Policy breaches
Operational risk
Amendments to the Policy
Procedures for Treasury Activities
Performance measurement
Commodity prices
Risk analytics

0 10 20 30 40 50 60 70 80 90 100

Chart 19: Respondents with treasury procedure manuals

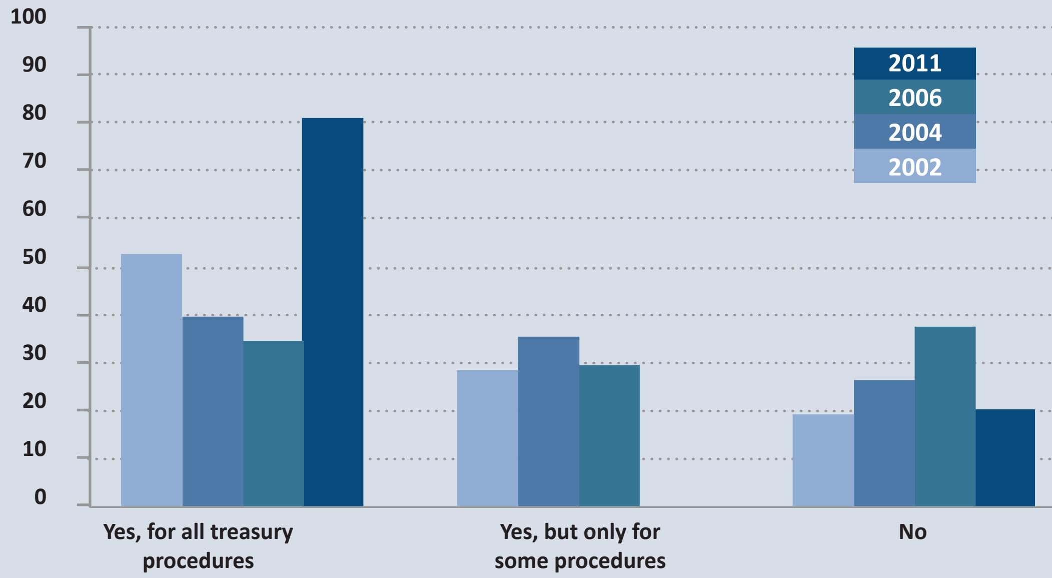


Chart 20: Segregation of duties

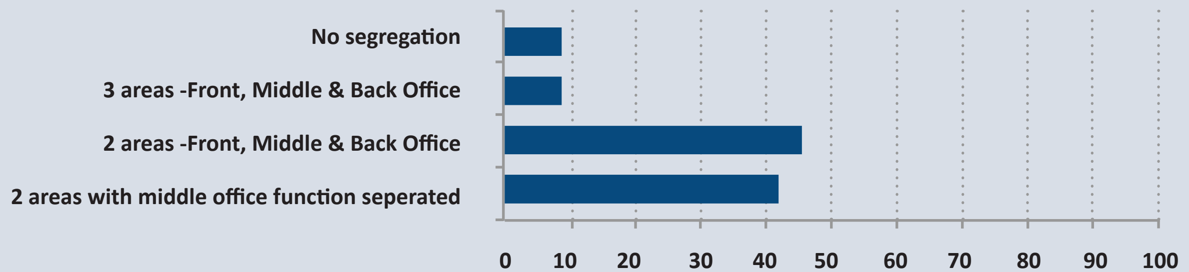
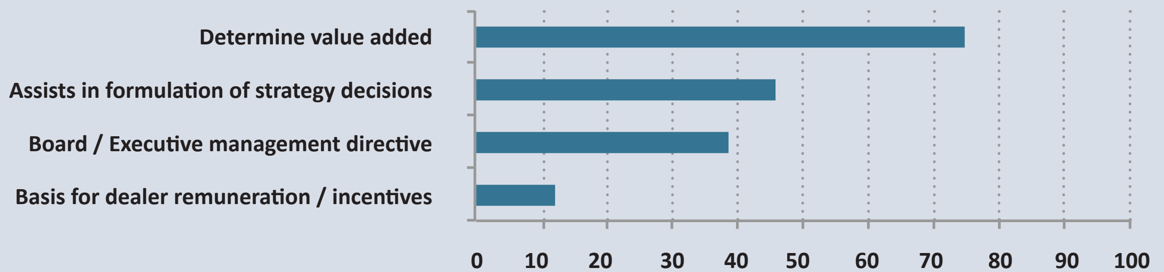


Chart 21 :Reasons for measuring performance



PERFORMANCE MEASUREMENT

The proportion of respondents who measure treasury performance has increased substantially in this survey to 61% (2006: 39%, 2004: 55%). The marked increase in performance measurement represents a return to (and above) levels seen in the 2004 survey. This may reflect the smaller average size of the participating companies in the 2006 survey.

The main reason for not measuring performance was that it was not necessary for the nature and size of treasury activities (50%). Other commonly reported reasons were that respondents did not believe it added value, or that they could not identify the appropriate performance benchmarks. For those who do measure performance, the main reasons include to determine the value added by treasury (74%), and to assist in the formulation of strategy decisions (45%). Refer Chart 21.

78% of respondents are satisfied with their performance measures (2006: 82%). The steady increase in this figure up until 2006 appears to have moderated. For respondents who were not satisfied with performance measures, the most commonly cited reasons were that the measures were still being developed, or they were either too complicated (30%) or too simplistic (30%).

As in previous surveys, the benchmarks most commonly used by respondents to measure performance were market rates or budgeted rates. The proportion of respondents who measure treasury operations performance has increased substantially to 72.5% (2006: 22%). Performance measures of operations were most commonly compared with last year's performance and budgeted performance.

TREASURY STRUCTURE AND STAFFING

94% of organisations have a separate treasury unit (defined as having a department or sub-unit with at least one person primarily involved in treasury-related activities), a significant increase when compared with 2006 (53%), 2004 (61%) and 2002 (70%).

Respondents were asked to classify their treasury (whether a separate unit or not) as either a cost centre (defined as passing on costs and profits to the business), a service centre (taking a fee to cover its costs and revenue/profits allocated to the business), or a profit centre (retaining costs and profits). The percentage of respondents classified as either a service centre or profit centre have declined when compared with 2006 (respectively, 2011: 11%, 2006: 15% and 2011: 8.8%, 2006: 13%) while more respondents now classify their operations as cost centres (2011: 80.2%, 2006: 72%). These results are shown below in Chart 22.

Survey participants were also asked how their treasury was positioned within their organisation. For the vast majority of respondents (92.2%), the treasury unit is located at the organisation's headquarters. For 6.7% of respondents the organisation's principal treasury unit is off-shore and 1.1% indicated that their organisation operated two or more specialist treasury centres that complement each other (e.g. treasury operations in one centre and corporate finance in another centre).

Finally, respondents were asked where their organisation's principal treasury unit was located. Australia dominated all other countries with a 91% response share. Other countries included New Zealand (3.4%), Europe/UK (4.5%) and USA (1.1%).

FUNCTIONS UNDERTAKEN BY TREASURY

Respondents were asked to nominate the functions for which their treasury is responsible (front, middle and back office). As expected, the two main functions currently undertaken by treasury are those of managing cash and liquidity and banking relationships. Chart 23 shows the percentages of functions undertaken by treasury.

Unlike the period of 2002-04 which saw increases in nearly all functions of treasury, the 2006-11 period presented irregular increases and decreases in some functions while others remained fairly stable. The biggest increase was seen in commodity price risk (9.4%) and the biggest decrease was seen in tax planning (-23.6%).

TREASURY STAFFING

Respondents were asked to indicate what their treasury staffing level was two years ago and presently. The most telling statistic is the continuing fall in one person treasuries (which was predicted in the 2006 report). Also as expected, staffing within the 2-3 and 4-8 brackets have increased compared to 2006 levels. Chart 24 shows the number of staff in treasury units.

A new question from the 2006 survey asked respondents what degree of difficulty they encountered in recruiting treasury staff. Up from 7% (2006), 12.5% of respondents who had recruited in the last two years found it easy to do so. 'Easy' was defined as numerous candidates with appropriate skill levels. 39.6% (2006: 22%) found it difficult (shortage of candidates with appropriate skill levels) while 47.9% had no need to recruit.

Chart 22: Classification of Treasury

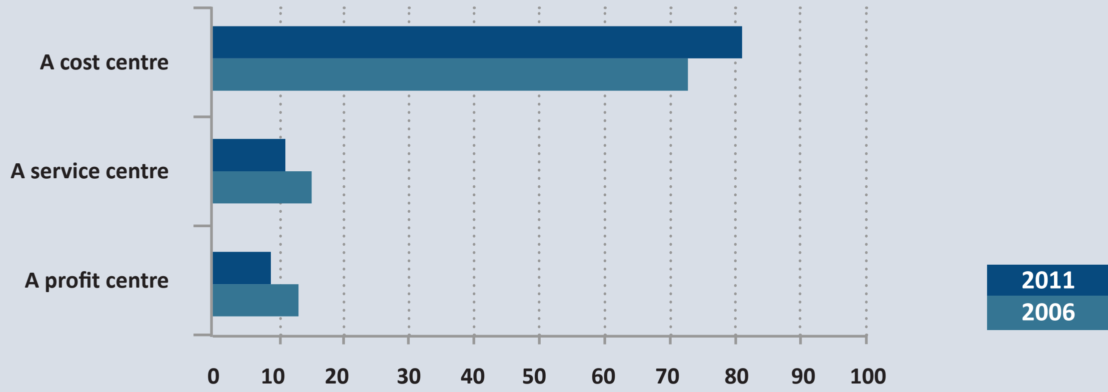


Chart 23: Treasury functions

2011
2006
2004

Tax planning
Non treasury credit risk
Reinvestment plans
Overall business risk
Equity raising
Strategic planning
Project evaluation
Dividend policy, share buybacks
Capital allocation
Commodity price risk
Insurance risk
Trade finance
Corporate finance/structured finance
Working captial
Accounting for treasury transactions
Derivatives disclosure in financial reports
Bank relationships
Cash and liquidity

0 10 20 30 40 50 60 70 80 90 100

Chart 24: Number of staff in treasury units

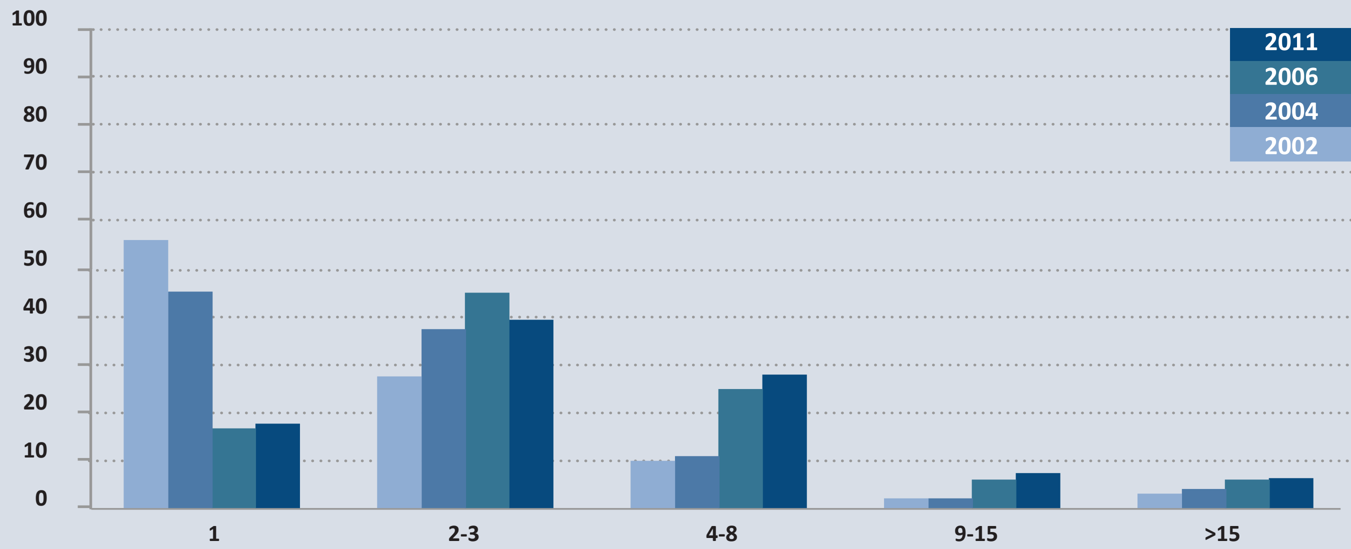


Chart 25: Expected Role in 5 years time

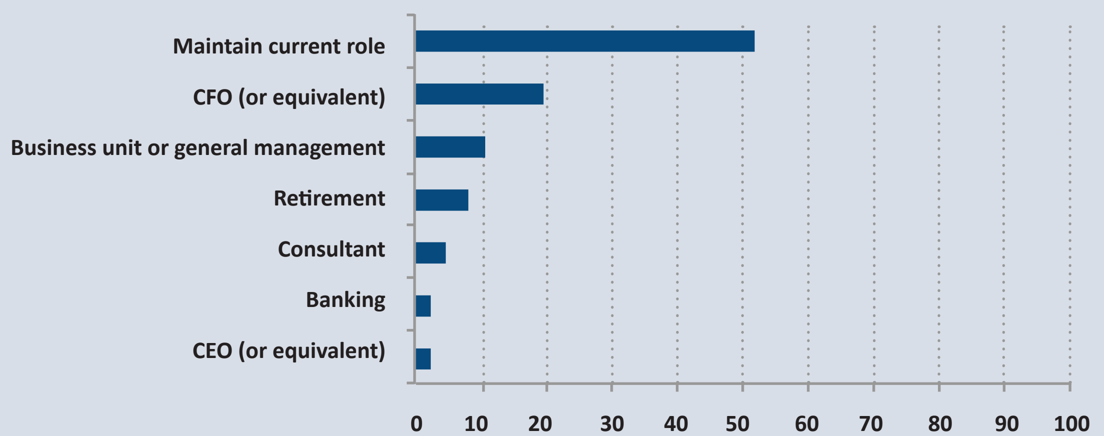
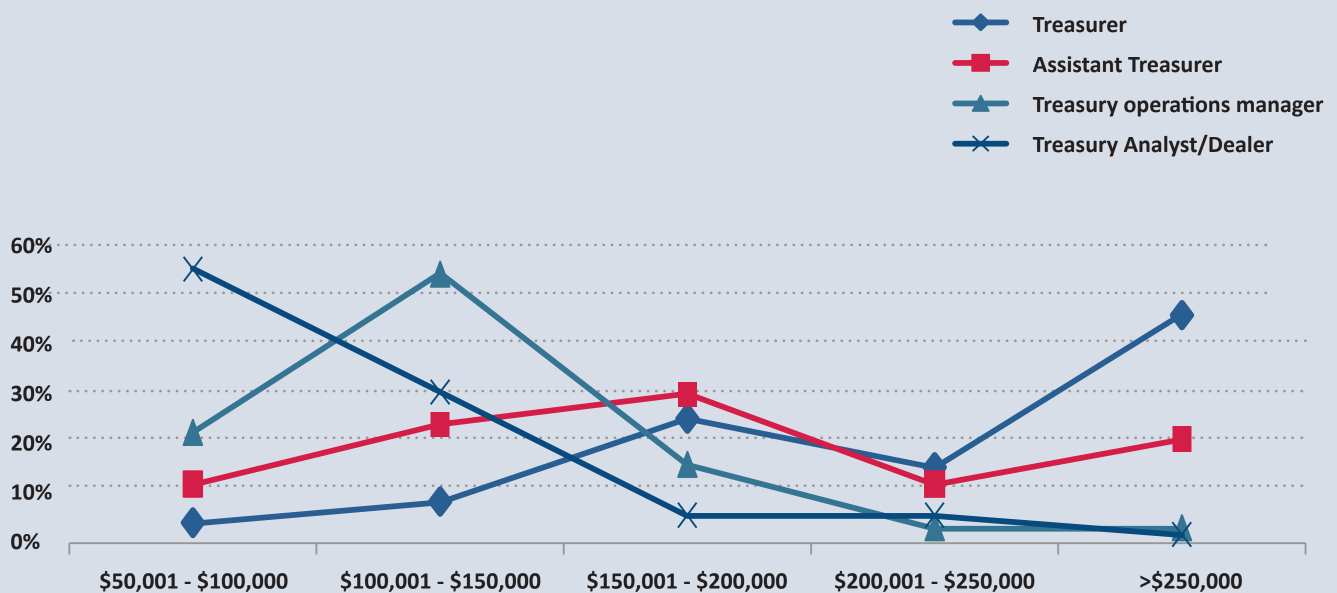


Chart 26: Treasury remuneration



TREASURER PROFILE

The profile of the treasurer remains largely unchanged from previous surveys. Treasurers are predominately male (86.2%) and aged between 41-50 years (37.2%). The percentage of female treasurers has remained approximately constant with 2006 levels (2011: 13.8%, 2006: 14%).

Current treasurers' previous work experience consisted of FRM/ treasury (67%), financial services/banking (18.2%) and corporate accounting/tax (14.8%). When asked what role they expected to be undertaking in five years' time, the majority of respondents replied that they would be maintaining their current role (52.3%). CFO (or equivalent) (19.7%) and business unit or general management (10.7%) were the second and third highest replies. Chart 25 shows the respondents expected role in five years' time.

TREASURER REMUNERATION

The remuneration of treasurers again increased compared to previous years, with 46.5% of treasurers earning in excess of $250,000 (2006: 35% earning excess of $200,000). Chart 26 shows the current distribution of the remuneration for treasury staff.

OUTSOURCING

19.1% (2006: 28%) of respondents have outsourced or intend to outsource functions from their treasury. The most outsourced functions are fund raising (33.3%) and management of liquidity, FX, IRR, counterparty or commodity or price risk, investments, deal execution, settlements and system administration (25%). Chart 27 shows the percentages of functions outsourced. The main driver for outsourcing was predictably cost efficiency (73.4%). Non-core function (13.3%) and inability to attract and retain specialists (13.3%) made up the minority of responses on this issue.

Chart 27: Functions outsourced

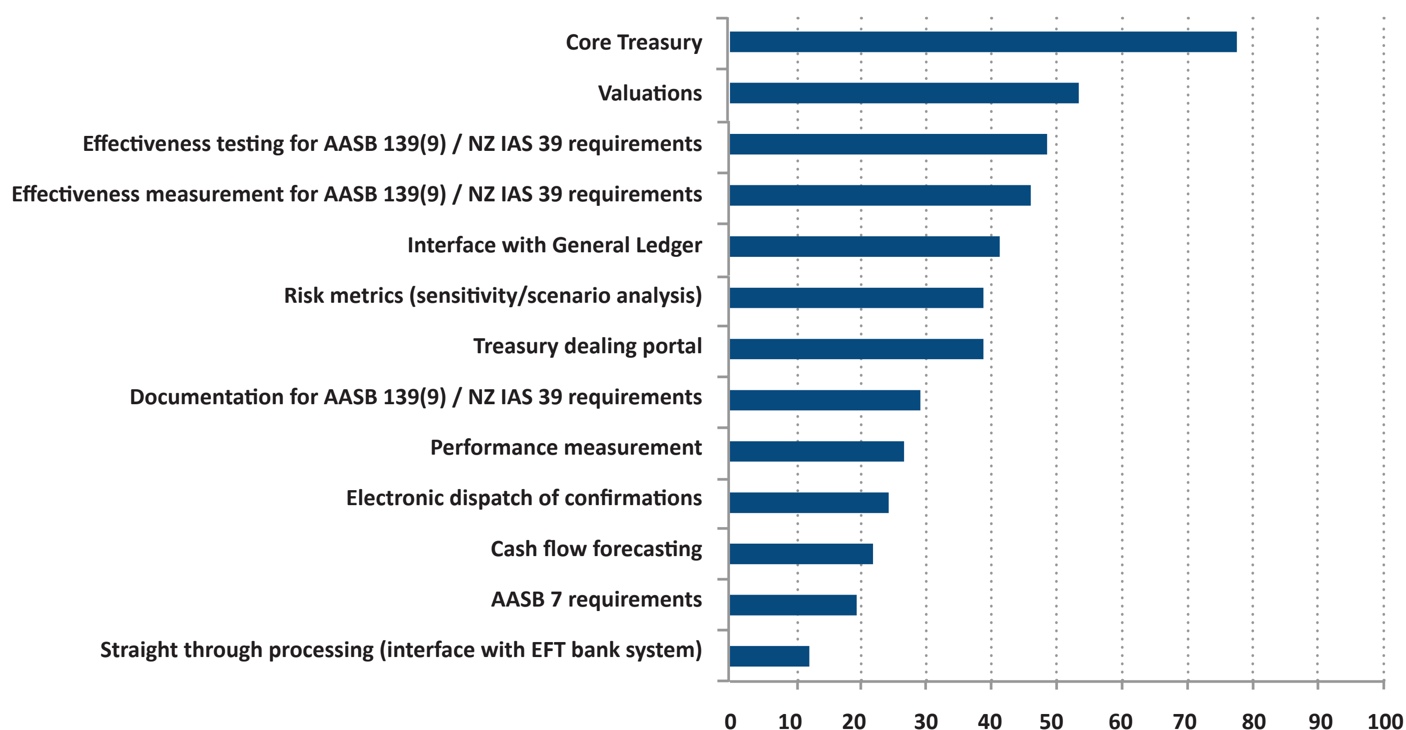
TREASURY SYSTEMS

The current survey asked respondents to indicate which main proprietary Treasury Management System (TMS) and valuation system their treasury uses. Integra-T, Quantum and Visual Risk were the systems used most by respondents with each system accounting for approximately one fifth (19.6%) of total responses. Conversely, a total of 19.6 % of respondents indicated their treasury did not have a main proprietary TMS and either did not plan on implanting one (10.7%) or was considering one in the next 2 years (8.9%).

Treasury functions which use TMS's (as indicated by respondents) included core treasury (78%), valuations (53.7%), Effectiveness testing for AASB 139(9) / NZ IAS 39 requirements (46.8%) and Effectiveness measurement for AASB 139(9)/NZ IAS 39 requirements (46.3%). The full range of functions are shown below in Chart 28.

When asked if they made full use of their TMS's functionality, an overwhelming number of respondents answered no (80.4%). More importantly, respondents were asked why if they answered no to this question. 48.4% answered 'Don't need all functions', 35.5% answered 'Some functions not suited to our organisation's processes and too costly to customise', 16.1% answered 'Some functions not user friendly' and 35.5% answered 'Inadequate training / staff knowledge of system'. These results indicate that firms might consider in-house developed systems along with more rigorous training programs as the increased costs (development of system and greater staff training) may be outweighed by a greater increase in benefits (increased efficiency).

Chart 28: Treasury functions which use TMS's



80.4%

of respondents answered no.

ACCOUNTING AASB 139/NZ IAS 39

There has been much time since the 2006 survey for firms to adjust and comply with AASB 139/NZ IAS 39 in relation to the recognition and measurement of financial instruments. Survey results indicated that most Treasury and Accounting/Finance business units share responsibility for complying with AASB 139/NZ IAS 39 requirements (55%). 23% of respondents indicated that the Treasury was solely responsible for compliance, while compliance was allocated to the Accounting/Finance unit for 22% of the respondents.

In the 2011 survey, respondents were asked about the impact of AASB 139/NZ IAS 39 on credit risk, commodity price risk, foreign exchange risk and interest rate risk. Consistent with the 2006 survey, most respondents reported no impact (2006: 60%), and this was especially pronounced in relation to credit risk (85%) and commodity price risk (83%). See Chart 29.

The results also reveal that whereas there was minimal impact on foreign exchange risk and interest rate risk (63% and 64% respectively), there were more changes to hedging strategies and treasury policies with regards to the latter two risks.

Interestingly, a relatively large minority (41%) of respondents also indicated that AASB 139/NZ IAS 39 had changed their ideal use of financial instruments for treasury risk management. However, for a majority of respondents (59%), use of financial instruments did not change with the implementation of the new standards.

An overwhelming majority of respondents (82%) used a Treasury Management System to value derivatives on their balance sheets. This was a large increase from the 18% of the 2006 survey respondents who were using a treasury system. Aside from core treasury functions, the systems were primarily used for valuation (54%), effectiveness testing (49%), effectiveness measurement (46%) and documentation (29%) for AASB 139/NZ IAS 39. The most prevalent systems were Quantum, Integra-T and Visual Risk (all with a respective share of 18%).

EMBEDDED DERIVATIVES

Recognition and measurement of embedded derivatives as required under AASB 139/NZ IAS 39 has improved since the 2006 survey, which may reflect adjustment and clarification of procedures. Of respondents who were impacted, 5% indicated that Treasury was not responsible and 21% were unsure of which department had responsibility (2006: 45% and 8% respectively).

Of the respondents that did recognise and measure embedded derivatives, 45% nominated the Treasury department as having responsibility (2006: 27%). Other business divisions were responsible for 29% of respondents. The survey results suggest more centralised responsibility for embedded derivatives. The large minority of respondents unsure of which department had had control over embedded derivatives is most likely attributable to the derivatives being embedded in contracts that are the responsibility of other departments.

HEDGE ACCOUNTING

The majority of respondents hedging interest rate (83%), foreign exchange (81%), commodity price (73%) and credit risk (69%) have qualified for some proportion of hedge accounting under AASB 139/ NZ IAS 39. See Chart 30. This compares favourably with the number of respondents who expected to qualify for hedge accounting in the 2006 (over 60%) and 2004 (over 70%) surveys.

In relation to the methodology employed to test hedge effectiveness, there has been a large increase in the use of the hypothetical derivative methodology (2011:58% vs. 2006: 11%) which is used to assess hedging relationships that are not 100% effective. Respondents also reported an increase in the use of regression/statistical techniques, (2011:45% vs. 2006: 22%), with a corresponding decrease in use of the dollar offset and matched terms methodologies (see Chart 31).

Chart 29: Impact of the adoption of AASB 139/NZ IAS 39

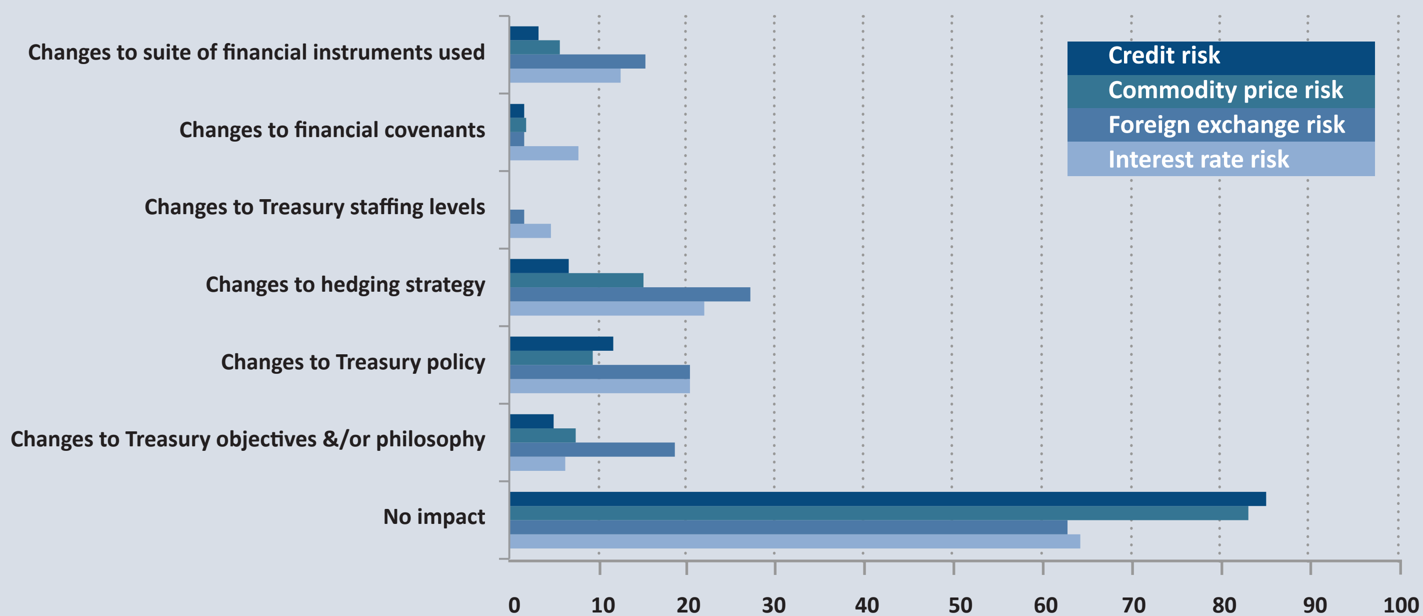


Chart 30: Proportion of hedges achieving hedge accounting under AASB 139/NZ IAS 39

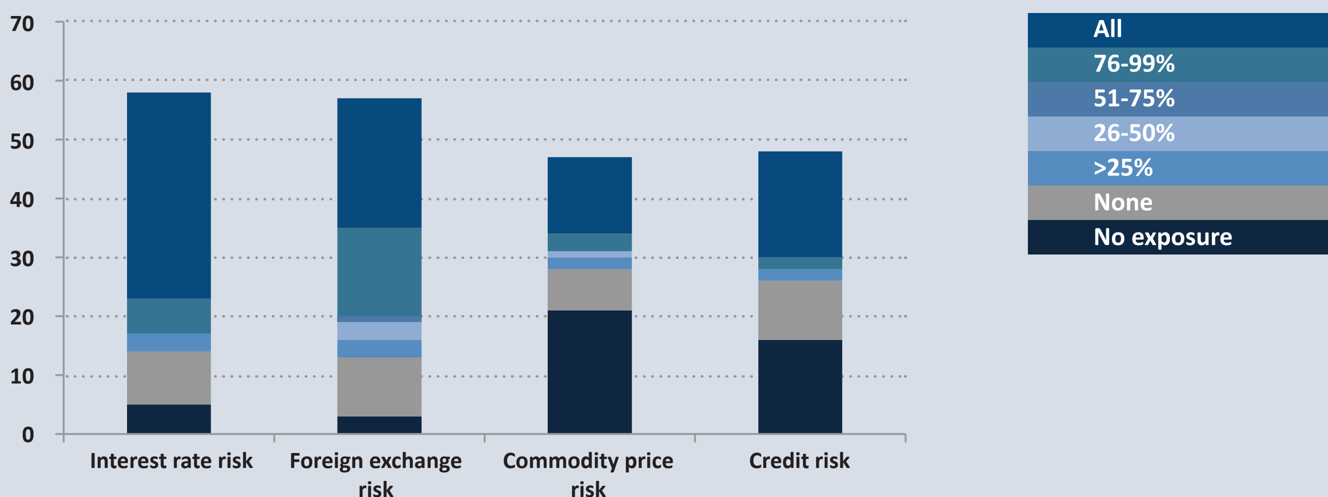
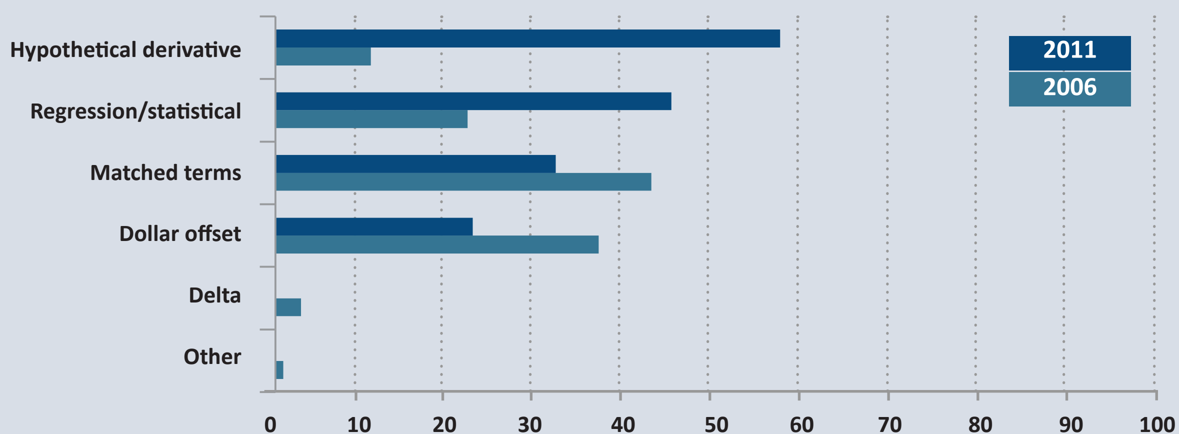


Chart 31: Methodology used to test hedge effectiveness



MAJOR ISSUES, DRIVERS OF CHANGE AND FUTURE DIRECTIONS

Treasurers were asked to identify the most important issue dealt with by treasury in the last two years, current drivers of change and their expected impact on operations over the next two years, as well as any proposals for changes to treasury operations.

MAIN ISSUES OVER THE PAST TWO YEARS

Unsurprisingly, a clear majority of respondents explicitly pointed to the global financial crisis and the associated impact on other areas of the treasury divisions as the main issue over the last two years. Treasurers particularly noted the fallout on liquidity and the difficulty of refinancing and access to funding in general.

Respondents also welcomed board recognition of the importance of balance sheet management, and expressed satisfaction at the fact that treasury departments are now integral to overall business risk management.

Aside from GFC-related issues, respondents also noted that compliance with AASB 139/NZ IAS 39, organisational restructurings and compliance with AASB 7/NA IAS 32 had led to changes in treasury policies.

As expected, this contrasts sharply with the 2006 survey, where it was found that the main issue was by far the requirements and implementation of AIFRS and AASB 139/NZ IAS 39. Other issues that increased in importance since the 2006 survey were liquidity management and foreign exchange volatility.

CURRENT DRIVERS OF CHANGE

Financing

Reflecting the altered, post-GFC environment, almost one quarter of respondents listed funding-related issues as the current driver of change in treasury management.

Treasurers expected this focus on funding to result in:

- Increased treasury management reporting to the board;
- A shift to focusing on improving relationships with lenders (as opposed to a price-focus);
- More conservative treasury policies;
- An increase in the cost of debt funding; and
- Greater transparency.

OPERATIONS AND TECHNOLOGY

The other key drivers identified by respondents were extracting operating efficiencies and technology.

Difficult and volatile market conditions for some respondents have meant that there has been an emphasis on the measurement and reporting of risk. This was likely to lead to more demand on treasury reports, greater focus on treasury performance, and investigation of better methods for hedging exposures, as well as looking to offshore hedging.

The increased demand on treasury functions is likely to lead to greater investment in technology to allow for more sophisticated measurement and pricing techniques and to integrate and improve current Treasury Management Systems. Many expect a broader role for treasurers and the accompanying greater scrutiny for the treasury function as a whole.

COMPETITIVE PRESSURES

Competitive pressures were another theme for several respondents, who highlighted that they were looking to extract operating efficiencies, especially from investments in technology.

Consistent with the 2006 survey hypothesis, it appears that treasury divisions are playing an increasingly strategic advisory role, rather than acting purely in a risk management capacity.

GOVERNANCE, ACCOUNTABILITY AND REGULATION

Consistent with increasing management focus on risk in organisations, a major driver of change is the increased demand on measuring and assessing risk. Many noted that there were significant positive effects for the organisation in general, such as greater knowledge of the business division, as well as increased knowledge of macro events that could affect operations. Respondents also noted the increased accountability that came with the focus on risk, but Treasurers saw this as an opportunity for the treasury to 'add value' to the company from the increased knowledge base.

However, the survey also revealed concerns that the increasing demands on Treasury input in companies with stronger risk management frameworks and the need to continually adapt to new regulations means the Treasury may lose sight of its original function. Although transparency was increased, respondents noted that they were spending much more time on compliance and reporting to the board.

For respondents who indicated that AASB 139/NZ IAS 39 had an impact on the ideal use of financial derivatives, there was an expectation of a move towards economic considerations rather than accounting policy driving the use of derivatives.

EMISSIONS TRADING SCHEME

Despite a relatively large number of respondents noting that the implementation of an emissions trading scheme would have an impact on their business, most companies indicated that the issue had not yet been addressed. This is unsurprising given the uncertainty surrounding the issue, and is supported by respondents highlighting the need for clear direction and legislation to be passed before the issue is addressed.

20% of respondents who identified a potential impact believed that the treasury would have some role when the legislation was expected to come into force.

Several Treasurers also noted that they expected most of the costs to be passed on to consumers.

PROPOSED CHANGES TO TREASURY OPERATIONS

Treasurers proposed the following changes to their treasury operations:

- Greater investment in technology with a focus on automation;
- Greater integration with other business units;
- Expanding staffing levels and improving/increasing training;
- More resources to properly fulfil expectations and demands on treasury; and
- Broader risk management responsibility.

ABOUT THIS SURVEY

BACKGROUND

This survey was conducted by the Finance and Treasury Association Limited and The University of Queensland. It is the tenth survey of its type begun in 1988 to identify and report on trends in corporate treasury activities. The survey was conducted from 1 November 2010 to 31 March 2011. Questionnaires were sent to organisations in Australian and New Zealand. This report summarises the findings from all respondents and aims to compare and contrast risk management practices across different industries and organisations by size as well as report on historical trends.

RESPONDENT PROFILE

The sample consists of 153 respondents, classified into twelve industries as shown in Chart 32. Chart 33 provides a breakdown of the respondents by revenue size. The current survey contained a significantly smaller sample of organisations with a revenue below $500 million (17.3%) compared with approximately 64% in 2006.

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Chart 32: Respondents by sector

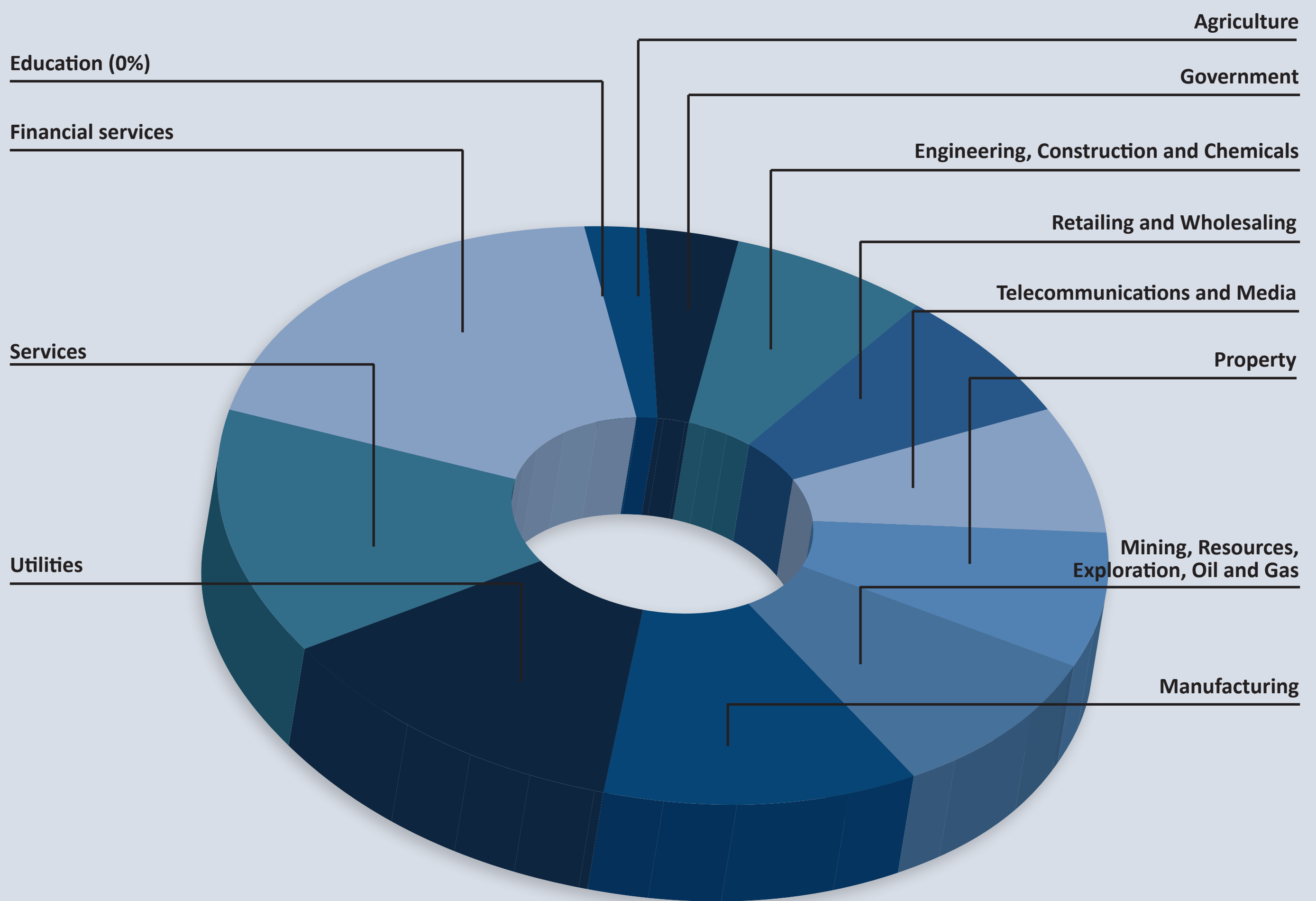
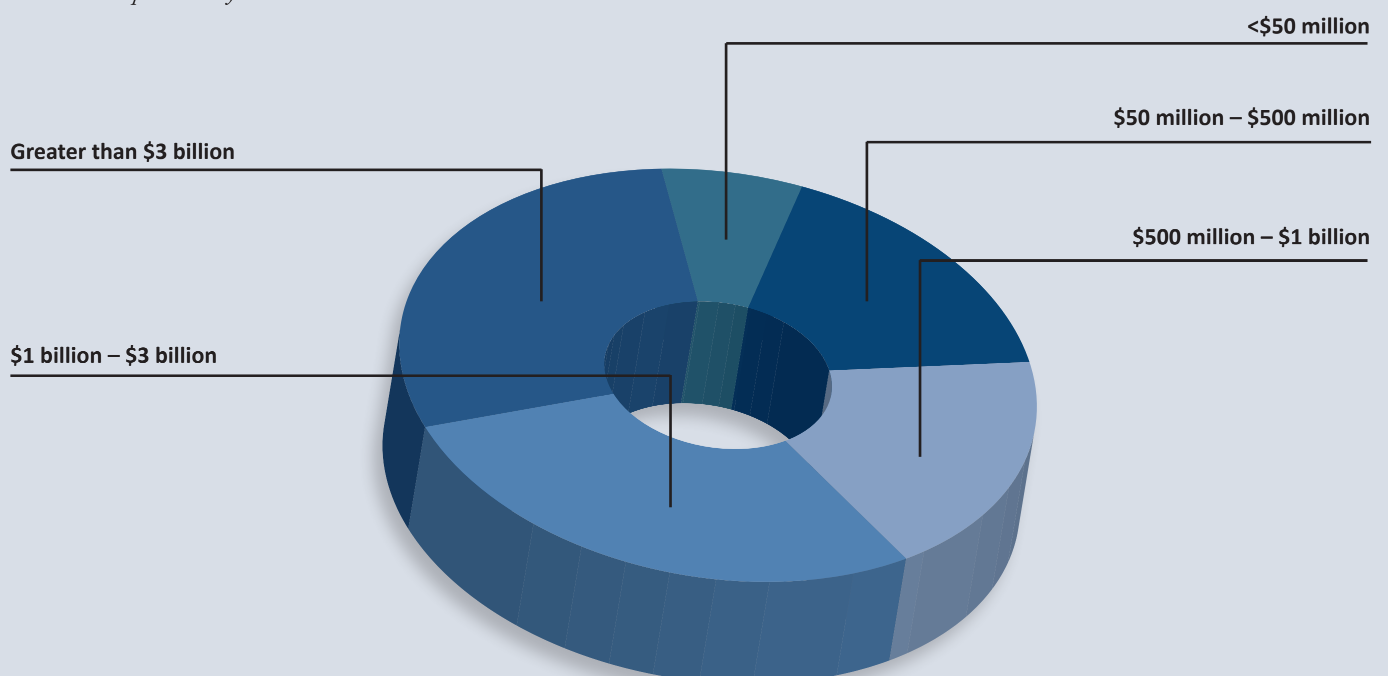


Chart 33: Respondents by revenue size



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