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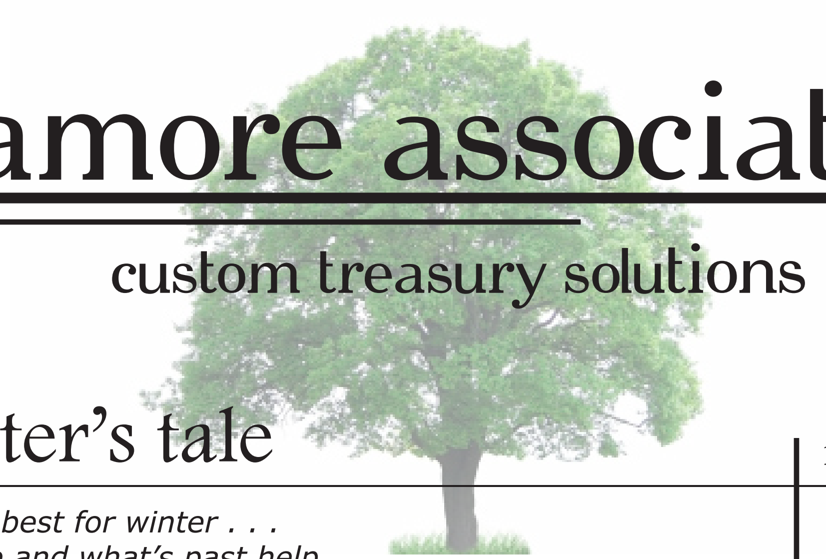
custom treasury solutions



a winter's tale

A sad tale's best for winter . . .
What's gone and what's past help
Should be past grief.

The Winter's Tale, 3.2

Winter, 2010. In the corporate world, no one is mourning the passing of the late year 2009. It saw many moments of grief, and for some companies, it brought job, benefit, salary, and numerous other losses large and small. But it's fading in the rear view mirror, and now it's time to start looking ahead.

Most of our clients have been doing so for a few months now, and although the picture is by no means clear, it is definitely a more positive view than 12 short months ago, when shell-shocked companies instituted wage cuts, suspended 401K matches, and took countless steps to bring costs down to meet the challenges of the global economic downturn. In retrospect, the times were every bit as bad as they felt: the worst downturn since the Great Depression. GM and Chrysler declared bankruptcy in March and June. No one knew when, or if, they would emerge. Banks struggled with both capital and liquidity, and borrowers felt the effects. Plans were revised downward, furloughs were offered, and uncertainty ruled the early summer of 2009.

From our vantage point, it seems like a very far cry from the current outlook, which is by no means irrationally exuberant. But what we see across the client base is positive:

- Companies reinstating the employee hours and benefits that were sacrificed last year
- Lots of acquisitive thinking
- Re-imagining projects that improve efficiency and profitability: gone are the "everything's on permanent hold" comments
- Evaluating strategic financial opportunities: more on this later
- Willingness to consider new initiatives
- And, finally, slow movement toward strategic new hires, although this is the last element to arrive, and it is by no means widespread

Welcome, Spring.

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repeat after us: cash is a corporate asset

We wrote about investment policy a year ago, and we are still fielding questions about investments, risk management, and uninsured exposures. So we offer here an update to our comments of a year ago. The theme still should be: Safety First.

One issue that many of our clients are addressing—with great vigor and trepidation—is investment policy. Even if, on average, a company is a net borrower, there is still cash around the system on a daily basis. With bank credit quality an urgent concern, now is a critical time to assess both where money flows and how any excess is invested (or otherwise managed). Risks abound, and some, while not exactly new, are freshly imbued with the shots and sound bites from bank failures, leaving depositors standing outside closed banks, noses pressed figuratively to the glass in search of assurances that deposits are safe.

So, some rules for this new road:

First rule of cash management: the objective is return of 100% of principal, NOT yield. Safety First! Repeat after me: cash is a corporate asset. This is a different investment strategy from managing your or any else's 401K. Right now no one needs to report losses on investments because we chased yield right into some Lehman fund and are now in line with the other unsecured creditors. Happily, this is one place the TARP and attendant legislation can help. In an effort to avoid more deposit runs on banks, the FDIC raised its insurance limit on all accounts to $250 thousand for any depositor. Some banks are also participating with the FDIC in a program that insures core deposits, non-interest bearing, to an unlimited level. This was originally intended to run through March of 2009, and has been extended to run through June 2010. The $250 thousand cap for interest-bearing deposits has been extended to 2014. Your bank must participate in the program, so make sure they do. All banks are seeking core deposits, so they're likely to readily offer up the information. Your benefit will be in credit earnings given to your relationship, not in any return, since this program doesn't cover any interest-bearing accounts. But do the math: with rates low, you can benefit in offsetting service charges as many banks have dramatically raised earnings allowance rates. That means: no CDs, no money market funds, no everyday interest funds, no repos, etc. Only non-interest bearing accounts. Period.

Second Rule: Know your banks. Take a quick look at debt ratings, market cap, and know Tier One capital ratios. This is handy to have in the file drawer when you get a call from the Board or CFO, and is worth an afternoon's time to compare. You may decide to recalibrate or rebalance investments or business as a result. You may decide that you are perfectly comfortable and each provider meets your standards for investments and balances. Either way it's a good exercise.

Third Rule: If you have international banks, consider consolidating with fewer providers. If there are many accounts, chances are some of your international banks have recently been (at least partially) nationalized. This is a great time to push the projects for transparency forward, consolidate international providers, and consider additional controls. We're spending a great deal of time on these projects and will happily provide more details if this is an area of interest for you.

Remember, cash is a corporate asset. That means reconsidering how frequently it sweeps to central accounts versus remaining at the subsidiary level. With the advancement of electronics, the need for subsidiaries or divisions to have cash around should be diminishing, not increasing. Reviewing the mechanisms for automating this movement, or establishing them if they are not currently in use, is highly prudent at this time. And this is working capital--putting it to more efficient use is not just good risk management, it's proper asset management.

the new normal in lending?

Well, what's happening here? We all know that 2009 was an awful year for borrowers. Banks struggled with tight credit and their own tight capital issues. Cost of capital became a featured part of each discussion with lenders. The "capital tax" for longer-dated transactions (and by longer-dated, we mean anything over 2 years) was onerous. Banks were preaching granularity, modest exposures, restraint, and moderation in risk profile and appetites. And amendments ruled supreme, accounting for over half of all 2009 banking transactions, according to ThomsonReuters. The band-aid became the normal approach to financing requirements in 2009.

So where do we stand today? The "new normal" is anything but normal. As the capital markets improved, starting with the investment-grade bond market in April-June of 2009, banks have slowly, and with accelerating velocity, begun to return to more lenient standards that generally favor borrowers more than in the past 18 months.

Generally, we are seeing 3 year deals in the investment-grade and near-investment-grade spaces. While many are talking about 5 year deals, not many are closing, and the price premium is meaningful. Covenants, also, are becoming looser, although that tends to be a case-by-case discussion. One exception to that is in the asset-based market, where a new tendency to add maintenance covenants (springing, but covenants nonetheless) to what have historically been covenant-free deals has emerged and persists.

However, and this is a big caveat, this is by no means a return to 2006. The underlying economic fundamentals, while improving gradually, (and thank heavens for that!) are still not robust enough to support this train independently. We estimate that around 30% of the capital active in the market in 2006, mostly via hedge funds and CLO's, has left the markets, at least for now, and some of that contraction may be permanent. While it is true that the banks are comforted by the extremely robust bond markets (including, in 2010, the high-yield market), they all retain recent memories of defaults and workouts abounding. Hence, news and events create more than their share of volatility. We believe that the improving banking markets are still subject to deal and industry-specific concerns. The banks themselves are also subject to a great deal of regulatory uncertainty (see the article in this issue about Basel 2) and that colors the nature of the risks they are willing to undertake.

So, the new normal is that case-by-case negotiation is alive and well. It behooves treasury and corporate finance professionals to solicit many data points when assessing the likely shape and structure of a financing. A myriad of views of "market" still apply, and clear-eyed analysis will benefit the company in this environment. While we believe conditions for borrowers will improve throughout the next several months, negative external events could send the markets backwards in a flash.

the news on basel: or, the regulator's revenge

A quick note to all our readers about Basel 2.75, or whatever you wish to name the version currently under review by the European regulators. The proposed version has been open for a comment period, which ended last Friday, April 16.

Generally speaking, the comments are expected to revolve around necessary changes to the proposed requirements for capital and liquid assets to be placed in support of unfunded loan commitments. Suffice it to say that the proposed requirements would negatively affect most borrowers, by requiring such onerous capital levels as to essentially put lending out of business as we know it today.

It remains to be seen what solution may eventually be proposed: however, it is clear that the mitigant to the Draconian measures put forward is the regulators' strong incentive to maintain the stability that we currently enjoy in the capital markets.

The impact of "Basel III" is murkier still, and potentially asymmetric, given the many geographies affected. US banks have not yet implemented "Basel II"; while Europe, Canada, Australia and others have already adopted it. Regardless, the changing capital requirements will ultimately have an impact on all.

international treasury: back in focus

A year ago, most of our clients knew that they did not know enough about their international treasury situation. But with budgets slashed and international banks being nationalized daily (OK, who owns our bank now? France? Belgium?) Treasury staffs just hunkered down and tried to keep the transactions flowing. That, amidst frequent calls for credit quality reviews by executive management and boards.

As the page turned to 2010, many of these same clients have taken a much more proactive stance to the monthly question, "why do we have borrowings out if we have $XXX million in accounts in Europe and AsPac?" We are currently engaged with several US-based multi-nationals in projects that will:

• Improve visibility and control of cash around the world
• Provide greater automation and cost savings for tedious manual processes
• Provide the means to optimize global working capital

Now is a terrific time to begin exploring what you can do to address these important and value-added initiatives for your company. In every case we have encountered, the benefits make a compelling value proposition. More details about current best practices are forthcoming in our next issue.

Welcome Christina Kmetko!
We are happy to announce our affiliation with Christina Kmetko, whose background in public accounting and external reporting serve her in her current practice, focused on investor relations and communications. More to come from Christy on these topics in future issues.

Ms. Kmetko can be reached at ckmetko@sycamoreassociates.com, or (216) 533 - 4651.

where in the world is sycamore?

Winifred Pinet recently traveled to Central Europe on a client project focused on international treasury. She also spoke at the February 2010 NEOTMA meeting on the topic "A Winter's Tale : Credit Markets 2009 and Trends for 2010"

Marcia Banks recently attended several symposia on credit risk and regulatory issues, including a meeting with the Chicago Fed.