Global Corporate Risk Management

Survey

BARCLAYS

July 2012

TREASURY, RISK
AND FINANCE
PROFESSIONALS
ACT

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Barclays/ACT Corporate Risk Management Survey

The survey highlights the shifting trends affecting corporate risk management and the increasing need for treasurers to focus on the quality of banking relationships and counterparty credit.

The survey received responses from over 100 multi-national companies. It highlights the major themes and trends in corporate risk management, particularly in light of events in the global financial markets since 2008, and builds on a similar survey done in 2010.

- The companies participating in the survey represent a broad range of regions, sizes and industry groups
- 79% of companies surveyed are from the EMEA region

An article highlighting the survey results was published in June 2012 in the Treasurer, the Official Magazine of the ACT - www.treasurers.org/thetreasurer

risk management
SURVEY

The heat is still on

THE 2012 BARCLAYS/ACT GLOBAL CORPORATE RISK MANAGEMENT SURVEY REVEALS THE ISSUES THAT TREASURERS ARE CURRENTLY FACING IN THE CONTEXT OF A CHALLENGING RISK ENVIRONMENT THAT HAS LOST NONE OF ITS DANGER AS THE FINANCIAL CRISIS CONTINUES.

At a headline level, the 2012 survey clearly shows that treasurers are focused on a broader range of risks than two years ago. Where transactional and operational issues used to dominate, strategic and macro-economic issues now top the list of concerns. The survey also indicates that, hand in hand with the economic outlook, treasurers are far more aware of counterparty credit risks and are demanding a better quality of relationship from their banking partners.

The 2010 survey highlighted four trends in risk management:

- a multiplication of risks for treasurers to manage;
- greater sophistication in treasury activity;
- an increased emphasis on relationship-led banking; and
- a growing recognition of treasury as a value generator, through active risk management approaches.

This year's survey shows that, for the most part, these trends have continued and remain hot topics. Since the financial crisis, treasurers are a lot more aware of the range of risks they need to manage, particularly in areas such as emerging markets, counterparty risk and market liquidity.

PACE OF CHANGE

Comparing the 2012 and 2010 surveys highlights a number of key areas where the risk management focus has intensified:

- Reducing earnings volatility has become even more clearly the top risk management objective for corporate treasurers; however, risk management as a value-added activity is still an important factor.
- Foreign exchange (FX) transaction risk is still the highest ranked risk management concern among treasurers.
- Over 40% of corporates are actively hedging emerging market FX risk and one-third of companies cite emerging markets as a driver of change in their risk management approach
- The level of concern over counterparty risk has become the third highest ranked risk management concern and corporates now put counterparty credit quality as the second most important factor when choosing banks for their risk management execution.
- Banking relationships have been simplified, with treasurers tending to do less segmentation of their banking partners by capability and increasingly asking all their core banks for support with risk management issues.

These changes at a policy and strategic level are arguably a direct result of the ongoing economic crisis. Anecdotally, corporate treasuries are becoming more sophisticated in how they manage their banking group, often using dynamic, market-based approaches in assessing which banks to transact with. Barclays regularly discusses issues such as liquidity, hedge portfolio composition and banks' own CDS (credit default swap) levels with clients, which is a significant change from only two years ago. Clients are increasingly more attuned to their counterparty exposures.

Additionally, the 2012 survey highlights how actual risk management practices have moved on:

- The mix of FX risks hedged is broadly similar, but with a decrease in balance sheet hedging and an increase in contingent risk hedging, such as risks linked to events including acquisitions or disposals.
- FX options are still a key risk management tool and, where used, treasuries are increasing their use of structured products to achieve their objectives.
- Emerging markets FX risks are now being hedged by a wider range of corporates, with over one-third actively managing these risks and often using a different approach from their exposures in G10 countries (France, Germany, Belgium, Italy, Japan, the Netherlands, Sweden, the UK, the US and Canada, with Switzerland playing a minor role).
- There has been a slight move to higher levels of fixed debt, but this is in the broader context of a lower rates environment. Vanilla swaps, cross-currency swaps and inflation swaps have all increased in importance.

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What lies ahead

The survey illustrates the changing priorities in risk management. We see a number of important challenges facing corporate treasuries:

- **increased awareness of counterparty credit**, encompassing credit line availability with banks and the creditworthiness of both banking and trading partners
- **a focus on emerging markets**, with treasurers needing to increase their risk management understanding of them as the world continues to look to these critical markets for growth
- **ongoing improvements in treasury capabilities**, with treasurers expected to have a real-time understanding of the risks facing their businesses and the real economic impact of those risks
- **adapting to new regulations**, with changes in the regulatory landscape for banks having a knock-on impact on corporate end-users which will need to be closely watched by treasurers

The survey was conducted during Q1 2012 by Barclays and the Association of Corporate Treasurers (ACT).

Survey findings

Risk management objectives and approach

The global economy and counterparty risk dominate treasurer concerns (see pages 5 to 10).

- **Reducing earnings volatility** has become even more clearly the top risk management objective for corporate treasurers
- **Foreign exchange (FX) transaction risk** is still the highest ranked concern, followed by **liquidity risk** and **counterparty risk**, which has become the third highest ranked concern
- 60% of companies surveyed stated that **market volatility** in some form is the biggest risk management challenge facing treasurers
- **Banking relationships** have been simplified, with treasurers tending to ask all core banks for risk management support
- Companies rank **counterparty credit quality** as the second most important factor when choosing risk management banks

'At a headline level, the 2012 survey clearly shows that treasurers are focused on a broader range of risks than two years ago. Where transactional and operational issues used to dominate, strategic and macro-economic issues now top the list of concerns. The survey also indicates that, hand in hand with the economic outlook, treasurers are far more aware of counterparty credit risks and are demanding a better quality of relationship from their banking partners.'

Rodolphe Alexis, Managing Director, Head of Corporate Foreign Exchange EMEA, Barclays Investment Banking, says: 'This survey clearly reflects the hot topics raised by our clients. Since the financial crisis, treasurers are a lot more aware of the range of risks they need to manage, particularly in areas such as emerging markets, counterparty risk and market liquidity.'

Source: Barclays. Note: Quotes taken from an article on the survey results, first published June 2012 in the Treasurer, the Official Magazine of the ACT.

Risk management activity

Risk management activity is increasingly driven by concerns over market volatility (see pages 11 to 19).

Foreign exchange risk management:

- **ongoing market volatility** is the largest driver of changes in FX risk management
- in line with the 2010 survey, around **half of companies use FX options** where FX risk is actively hedged
- hedging of **emerging market FX** risks has increased to **over 40%** of companies
- almost two-thirds of companies use some form of **e-commerce** for FX transactions

Interest rates risk management:

- there has been a shift towards **more fixed debt** over the last year, with **vanilla swaps** becoming an increasingly important hedging tool
- **inflation swaps** have also increased in importance
- **hedge co-ordinators** are used by 18% of companies and achieving optimal pricing is the main driver of this

Hedge accounting is recognised as an important factor in choosing hedging solutions, but for the majority of companies it **does not dictate the hedging approach.**

These changes at a policy and strategic level are arguably a direct result of the ongoing economic crisis. Anecdotally, corporate treasuries are becoming more sophisticated in how they manage their banking group, often using dynamic market-based approaches in assessing which banks to transact with.

Keith Gilmour, Director, Head of UK Major Corporate FX, Barclays Investment Banking, says: 'We regularly discuss issues such as liquidity, hedge portfolio composition and banks' own CDS levels with clients, which is a significant change from only two years ago. Clients are increasingly more attuned to their counterparty exposures.'

Source: Barclays. Note: Quotes taken from an article on the survey results, first published June 2012 in the Treasurer, the Official Magazine of the ACT.

Survey results

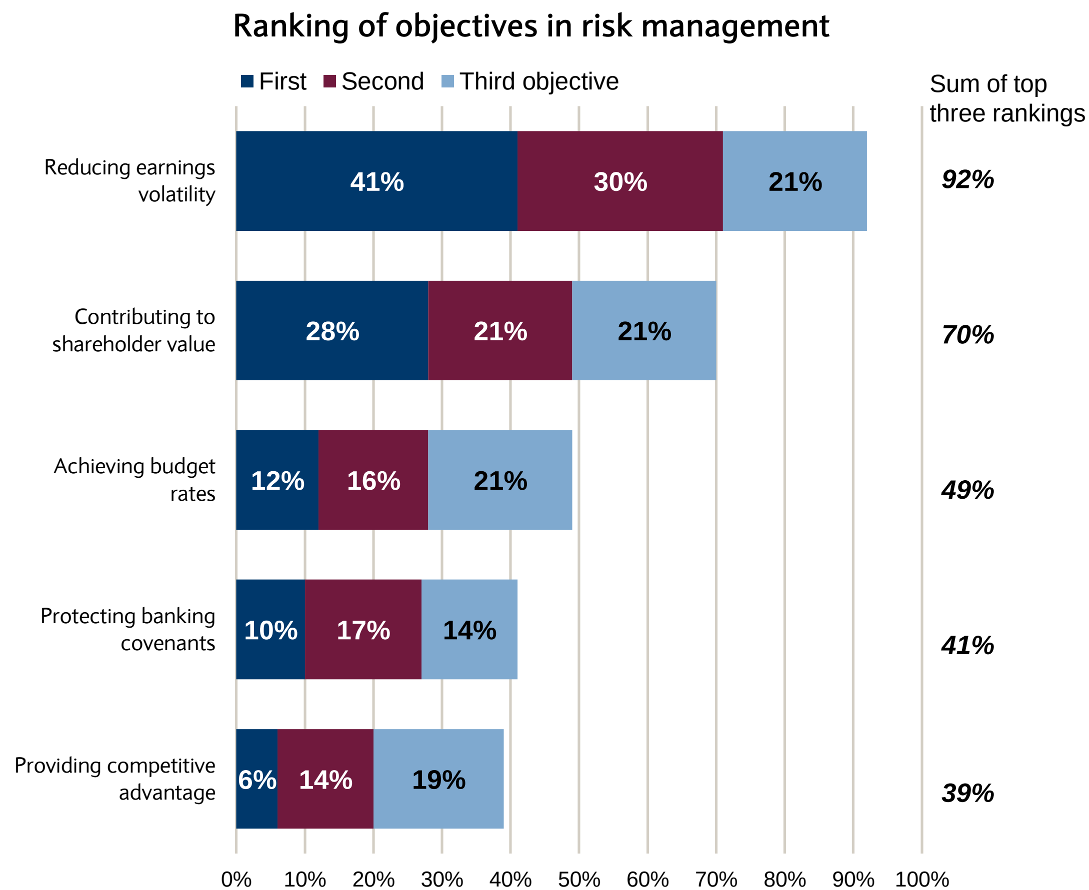
Risk management objectives

When asked to rank risk management objectives, earnings volatility and shareholder value are key factors.

- 92% of companies rank 'reducing earnings volatility' as a top three risk management objective
- 41% rank it as their number one concern
- Over two-thirds rank contributing to shareholder value in the top three
- This stands out as an important focus for treasurers

Additional participant comments

- Reduce:
  - credit risk
  - exposures
- Protect:
  - economic value
  - liquidity
  - cash flow
  - debt cost volatility

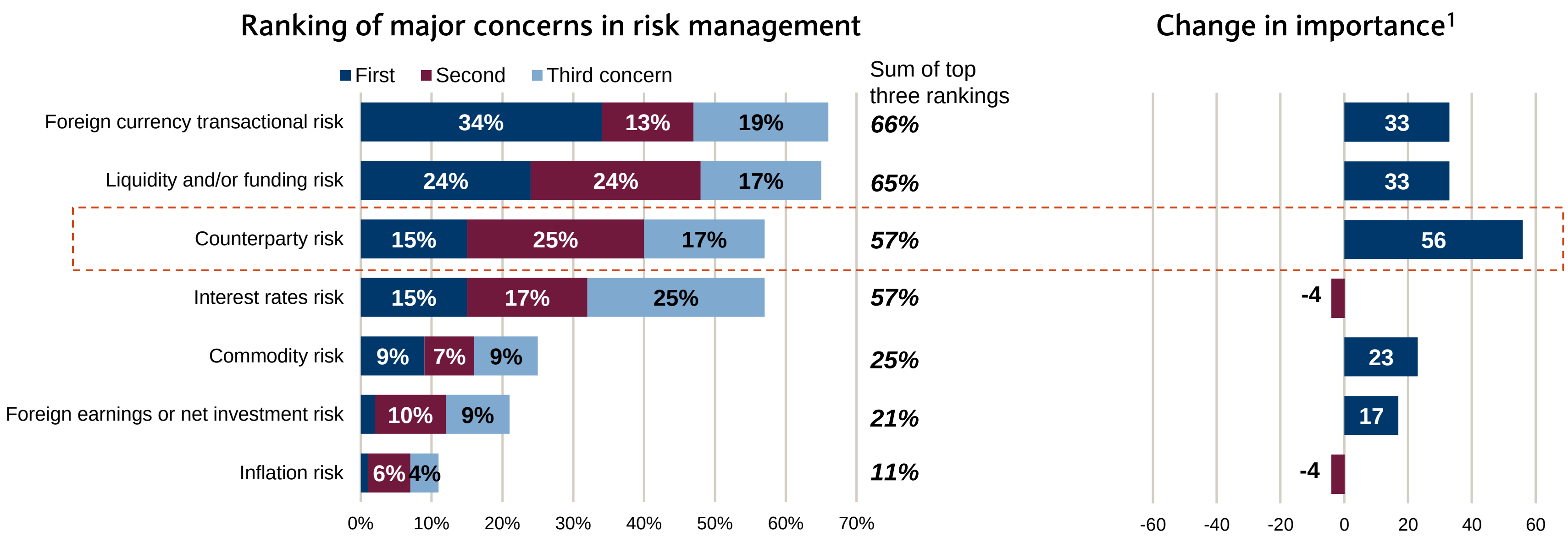


Source: Barclays.

Risk management concerns

When asked to rank risk management concerns, foreign currency transactional risk remains the primary concern, with liquidity and counterparty risks also a factor.

- 66% of companies rank **foreign currency transactional risk** as one of their top three concerns, with 34% ranking it as number one
- Liquidity and/or funding risk is the next highest ranked, and is a top three concern for 65% of companies
- Counterparty risk (i.e. credit quality of counterpart institutions) stands out as the third highest concern. In the 2010 survey, counterparty risk was fourth highest with 27% ranking it in the top three
- When asked to rate the change in importance of risk management concerns compared to one year ago, counterparty risk shows a marked increase in the level of importance for companies. The only risks which appear to be slightly less of a concern are interest rates and inflation risks, though only by a marginal amount



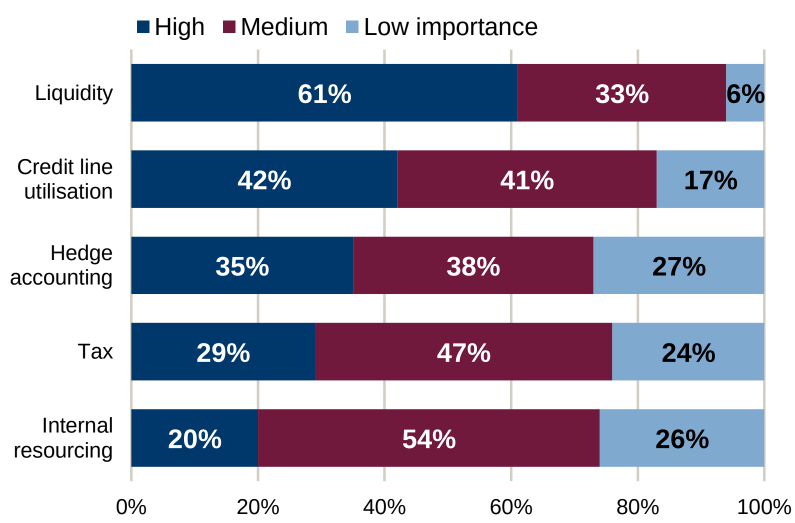
Source: Barclays. 1: Calculated as the percentage of respondents stating 'more concerned' less the percentage stating 'less concerned' about each issue.

Risk management considerations and challenges

Liquidity and credit lines top the list of key considerations, while global market volatility stands out as the biggest challenge.

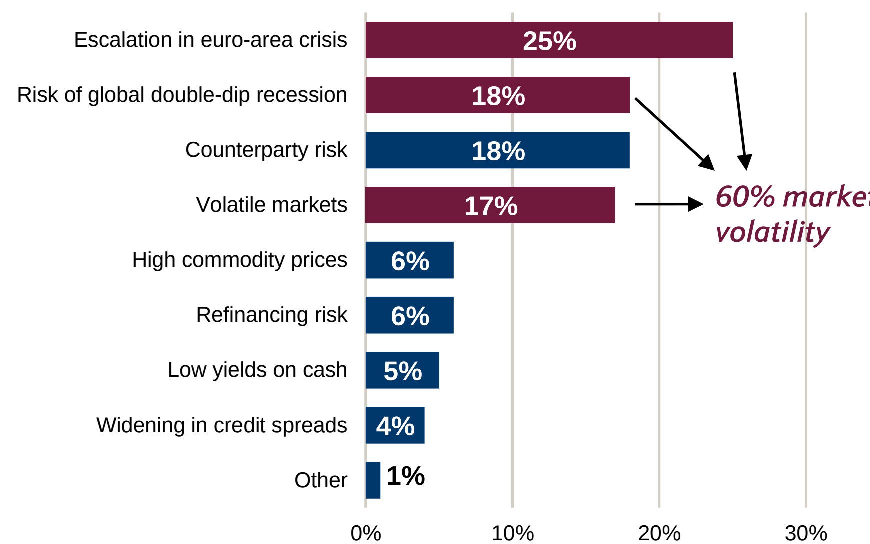
Risk management considerations

- Companies were asked to rate the importance of various considerations (other than price) when implementing their risk management strategy
- Liquidity is clearly the most important consideration, with 94% of companies rating it of high or medium importance
- Credit line utilisation is rated as the second most important consideration



Biggest risk management challenge in 2012

- 25% of companies surveyed rank an escalation in the euro-area crisis as the biggest risk management challenge in 2012
- Combining this with continuing volatile markets and the risk of a global double-dip recession, the survey shows that **60% of companies are focusing on these large, strategic challenges**
- Nearly one in five of companies cites counterparty risk as the most important market-driven concern



Source: Barclays.

Requirements of risk management providers

Companies are careful in selecting which banks to work with and require global international banks with geographical presence.

When approaching banks for risk management requirements, companies use a range of approaches.

- 48% of companies approach all banks for all their needs, an increase on the 2010 survey (40%)

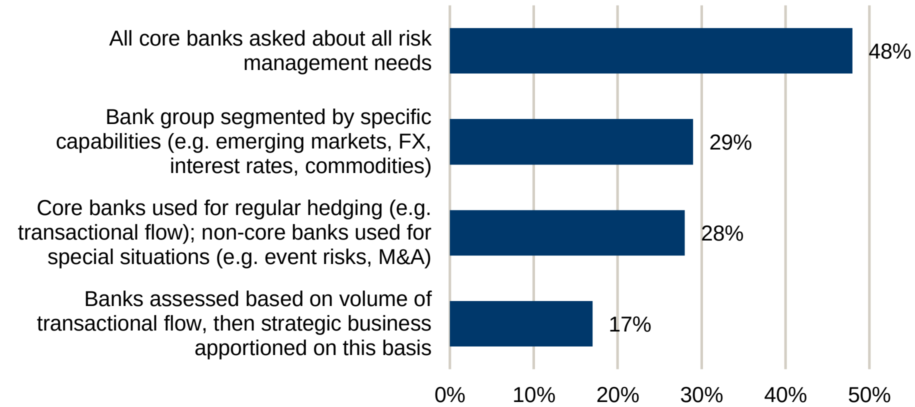
Segmentation of banking counterparties is relatively common:

- 29% segment banks by specific capabilities in different markets
- 28% of companies split their groups between core and non-core banks, used for regular activities and special situations respectively
- a small proportion (17%) use a volume-based approach to select their banking group

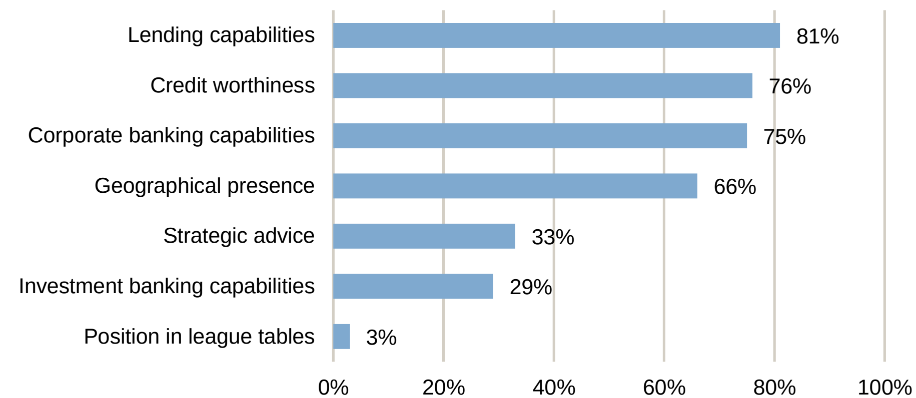
In terms of requirements of their core banking group:

- lending capabilities is the top requirement, with credit-worthiness second
- corporate banking capabilities and geographical presence are also important requirements

Use of banking group for risk management[1]



Requirements of core banking group[1]



Source: Barclays. 1: Respondents could select multiple answers.

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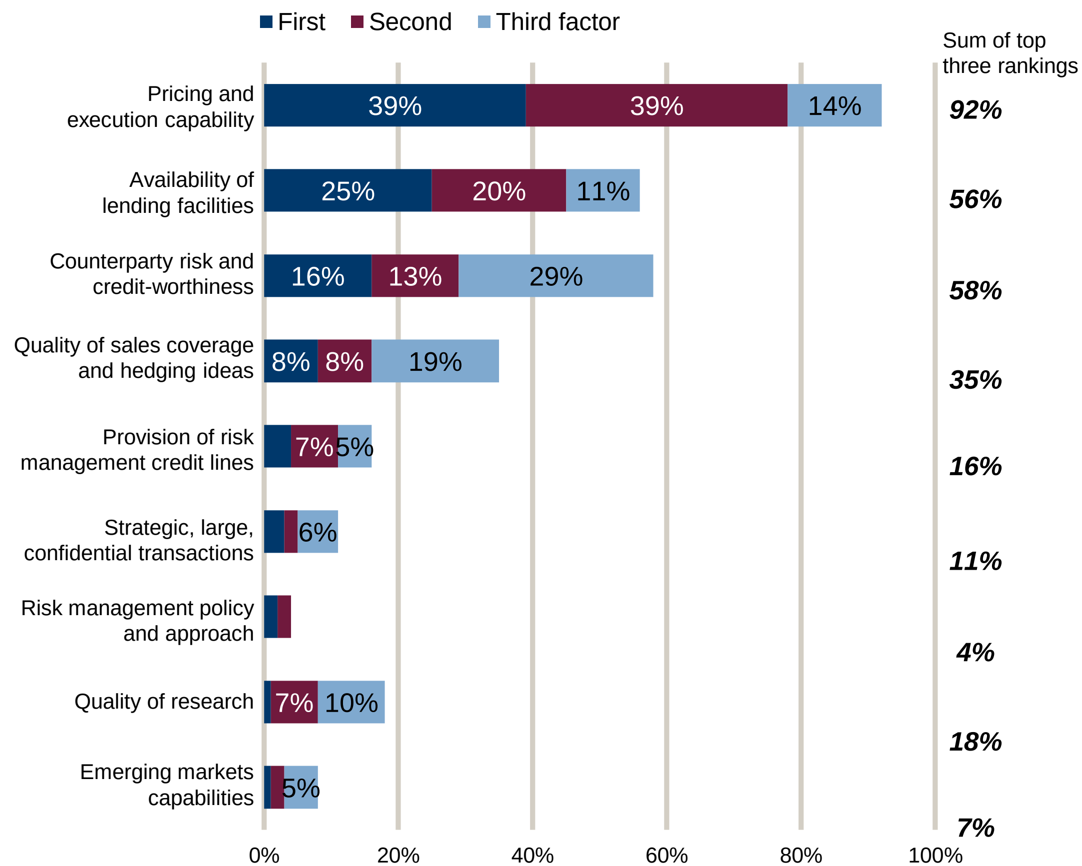
Choice of risk management provider

Pricing remains the most important factor when choosing risk management providers. Availability of lending facilities and counterparty risk are a close second group of considerations.

When approaching banks for risk management requirements, companies use a range of approaches:

- 'pricing and execution capability' is cited as the main factor in choosing a bank by 39% of companies, with 92% stating it as a top three factor
- the second group of factors are 'availability of lending facilities', and credit and counterparty risk, a top three factor for 56% and 58% of companies respectively
- a number of factors are low on the list of priorities when choosing which bank to use, suggesting that these factors are only considered for specific, special situations:
  - emerging markets capabilities
  - risk management policy and approach
  - strategic, large, confidential transactions (e.g. M&A situations)

Ranking factors in choosing risk management providers



Source: Barclays.

Additional risk management services

When asked to identify services that would bring benefits to a company's risk management, market information tops the list.[1]

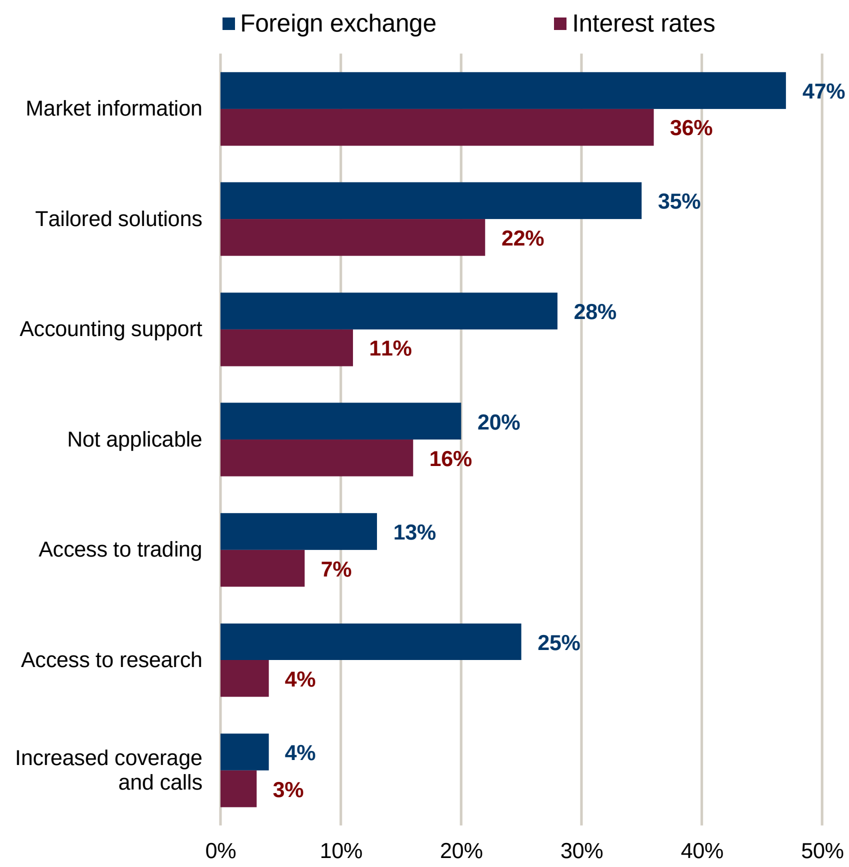
Companies clearly identified the areas that they feel are most valuable from their banks.

- **Market information**: timely and appropriate levels of information appears to be the most valued service, with a need for 'opinions on economic data' cited by one respondent
- **Tailored solutions**: companies identified a 'requirement for advice on larger trades', suggesting the need for a closer dialogue in strategic scenarios
- **Accounting support**: as accounting rules change and companies become increasingly aware of accounting restrictions, there is demand for guidance on this complex topic

There does not appear to be demand for increased coverage and access to trading or research.

This suggests that existing levels of coverage received by companies is about right, but that coverage could potentially be more focused in terms of content and timeliness.

Ranking factors in choosing risk management providers



Source: Barclays. 1: Respondents could select multiple answers.

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Foreign exchange risk management

Forecasted transaction risk is the most commonly hedged risk; balance sheet, earnings translation and contingent risks are hedged by a significant proportion of companies.

The companies surveyed represent a broad spread of FX transactional volumes.

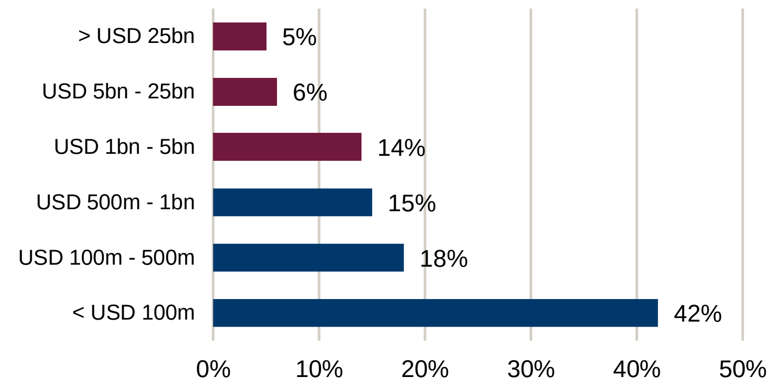
- 58% of companies have annual FX volumes of over USD 100m, of which 25% have volumes of over USD 1bn

Forecasted transactions are the most commonly hedged FX risks, with almost three-quarters of companies hedging this risk.

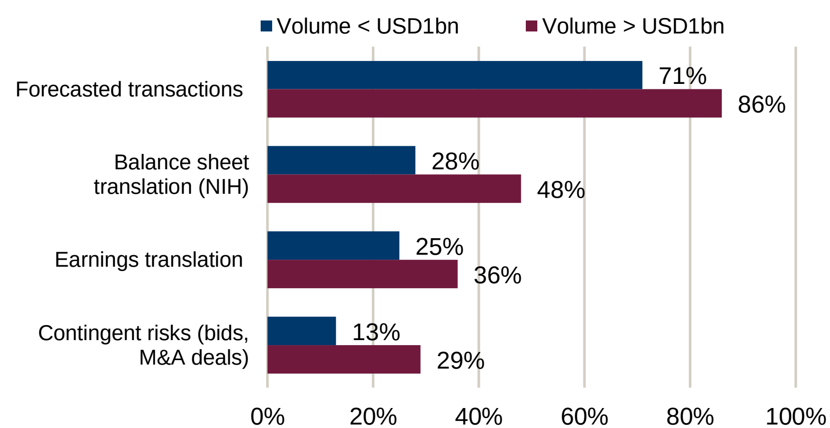
- One-third of companies hedge balance sheet translation risk
- Just over one-quarter of companies hedge earnings translation risk
- Around one-fifth hedge contingent risks

Companies with larger exposures (over USD 1bn) appear to be more active in the range of risks that they hedge.

Size of annual FX volume transacted



Hedging of foreign exchange risks[1]



Source: Barclays. 1: Respondents could select multiple answers.

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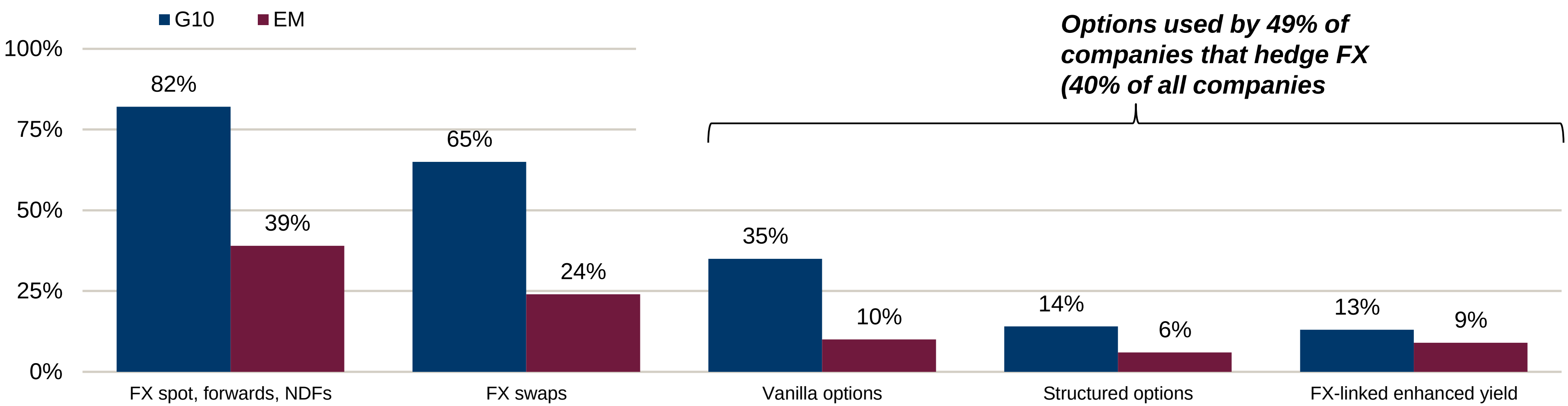
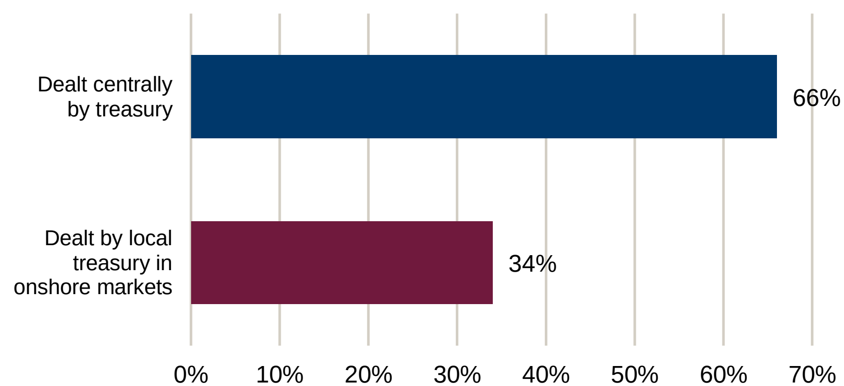
FX hedging instruments

Use of FX options is common in G10 currencies and growing in EM currencies.



- FX spot, forwards and swaps are the most commonly used hedging instruments
- For companies that actively hedge (82%), around half of them use options. This represents 40% of all companies surveyed
- Hedging of emerging market currency exposures is growing, though is still far less common than for G10 exposures
- Just over one-third of companies allow onshore dealing of emerging markets currencies by local treasury teams

Emerging markets exposure



Source: Barclays.

Changes in FX risk management

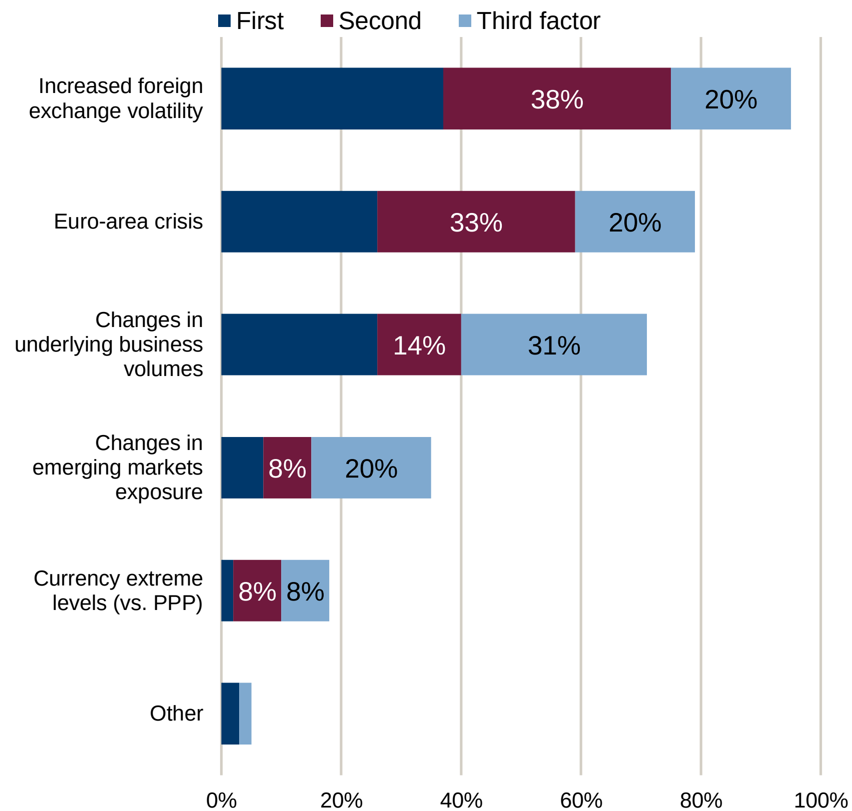
External market factors appear to be the main drivers of change in risk management activity over the last year.

- Increased foreign exchange volatility is a top three factor for 95% of companies surveyed
- The second most important driver is the ongoing euro-area crisis for 79% of companies, which is arguably linked with the increased foreign exchange volatility
- Changes in underlying business volumes ranks third most important factor, with 71%
- Emerging markets exposures and extreme currency valuations do not appear to be key drivers of change in risk management approach

Additional participant comments on factors driving changes to FX risk management:

'Credit lines'
'Change of hedging policy'
'Sale of subsidiary'

Ranking of factors driving changes to risk management[1]



Source: Barclays. 1: Respondents could select multiple answers.

Use of e-commerce for FX

Use of e-commerce platforms has marginally increased since 2010.

- 63% of companies surveyed are using an e-commerce solution to execute foreign exchange deals:
  - usage of e-commerce has grown since 2010 (vs. 61% in 2010)
- E-commerce penetration may be reaching a peak; however, there is growth in the use of automated FX payment systems
- Where companies do not want to increase their use of e-commerce platforms, the key drivers are low frequency of trades and a continuing preference for voice trading

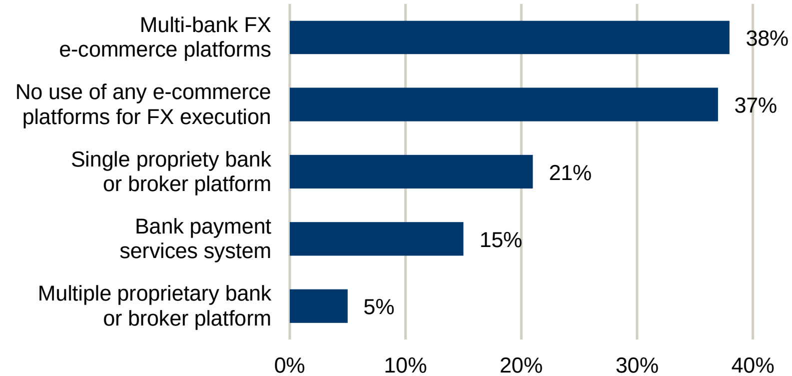
Additional participant comments on reasons for not using e-commerce platforms:

'Insufficient market liquidity for EM currencies'

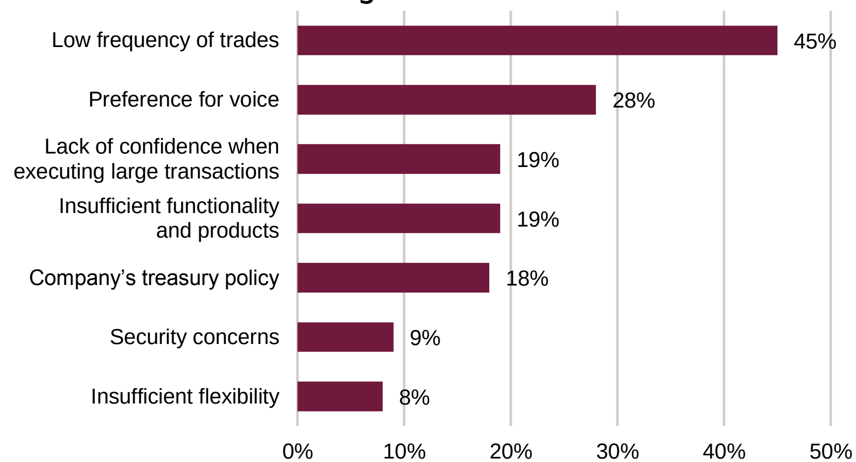
'Pricing availability for longer-dated trades'

'Prefer to discuss significant trades over the phone'

Use of e-commerce platforms



Reasons for not using e-commerce



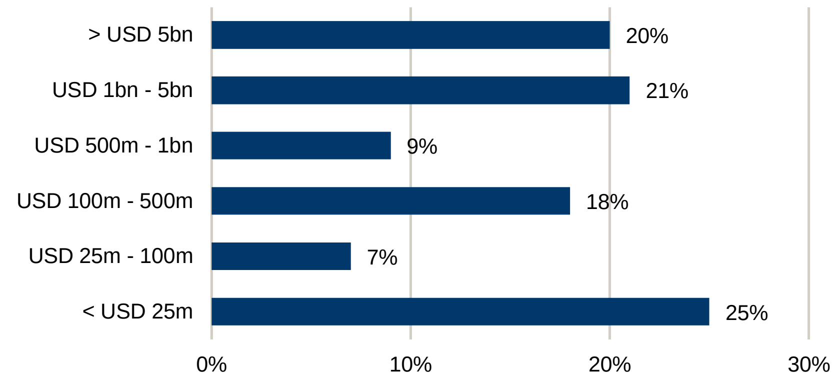
Source: Barclays.

Interest rates risk management

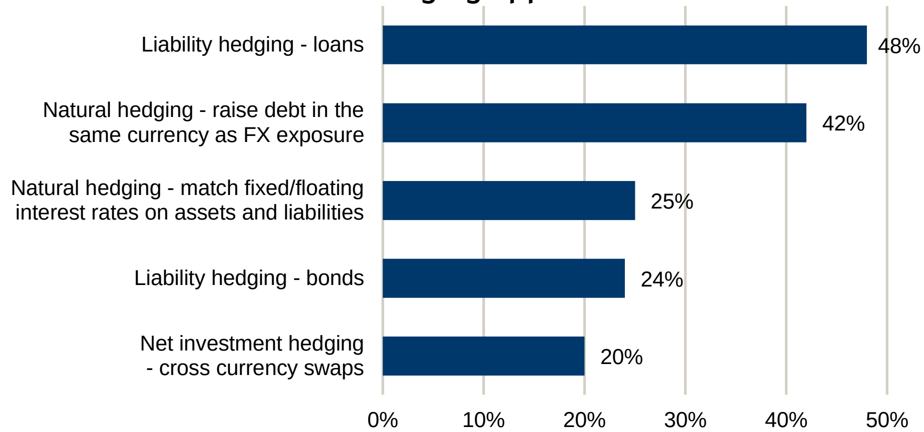
Companies surveyed had a broad range of debt size, with a range of hedging approaches.

- Over 40% of companies surveyed have debt of over USD 1bn, and one-quarter have debt less than USD 25m
- There is no typical mix of fixed vs. floating debt ratio; however, there has been a slight shift to more fixed debt since 2010
- A variety of hedging approaches is used, with no one approach dominating

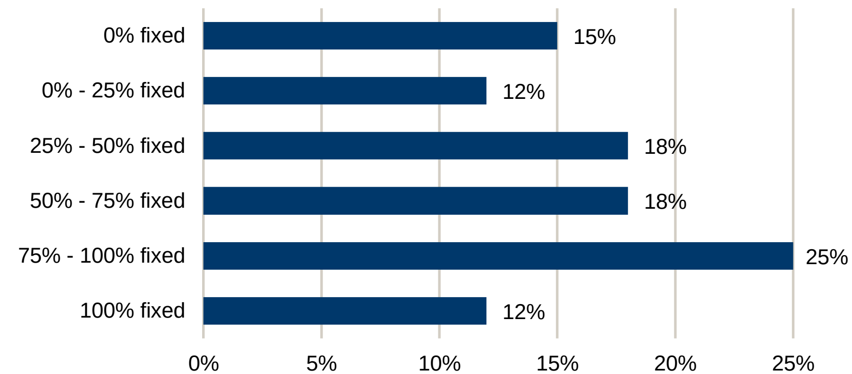
Size of company debt



Interest rate hedging approaches[1]



Split of fixed vs. floating debt



Source: Barclays. 1: Respondents could select multiple answers.

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Interest rates hedging solutions

Vanilla swaps and cross-currency swaps are the dominant solutions used.

60% of companies use vanilla swaps for their interest rate hedging.

- 24% use cross-currency swaps
- Vanilla and structured options are less used, but more than one-fifth of companies use options of some kind
- Inflation swaps are used by almost one-tenth of companies

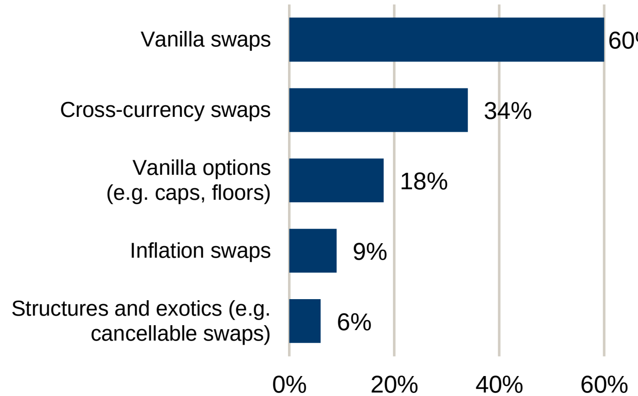
In terms of change in importance, inflation, cross-currency and vanilla swaps have all increased in importance over the last year, while structured, exotic options have decreased in importance.

Key reasons for any change in hedging activity are:

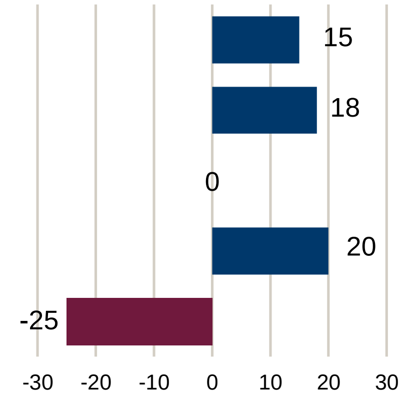
- changes in debt profile – for example, shift from bond to bank debt, reduced tenor
- underlying market levels

Counterparty credit and credit availability are less important factors.

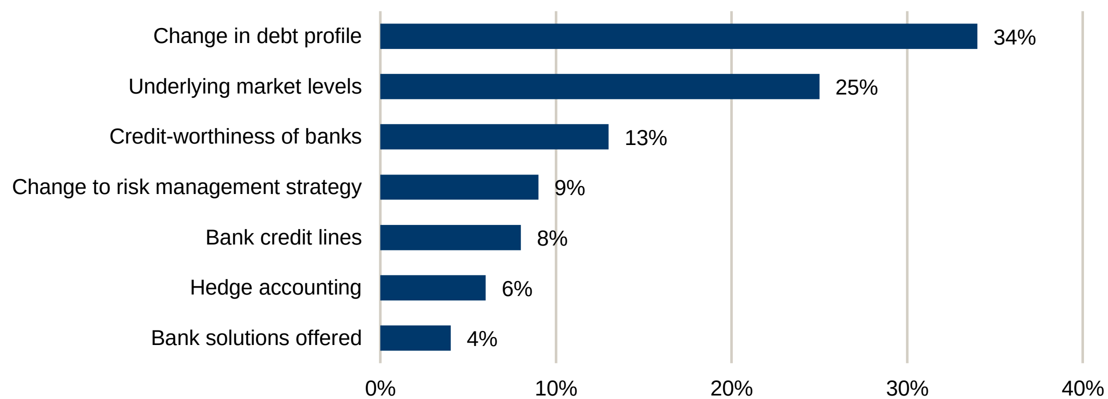
Hedging solutions used[1]



Change in importance[2]



Reasons for change, if any, in hedging activity[1]



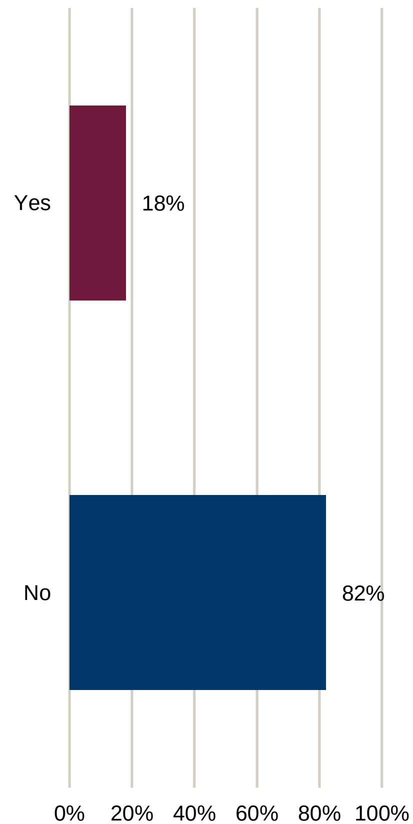
Source: Barclays.
1: Respondents could select multiple answers. 2: Calculated as the percentage of respondents stating 'more important' less the percentage stating 'less important' about each issue.

Interest rates and the use of a hedge coordinator

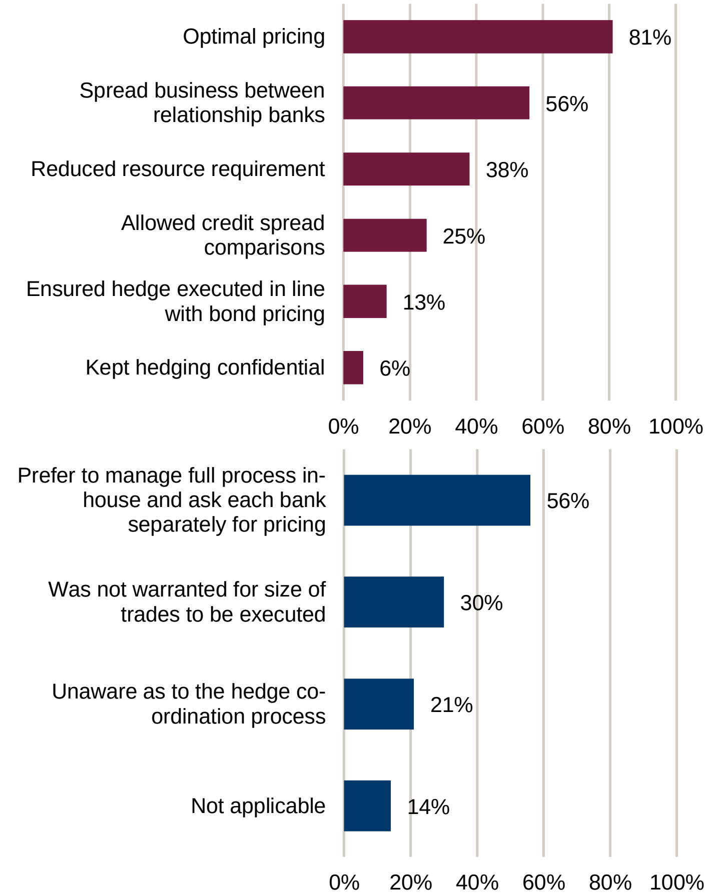
Hedge coordinators have been used by 18% of companies surveyed, with optimal pricing the main driver of usage.

- 18% of companies surveyed have used a hedge coordinator or hedge syndication process for their interest rate hedging in the past
- Where a hedge coordinator has been used, the primary reason given is that it provides optimal pricing across a broad bank group
- Confidentiality of hedging is a less important factor
- Where a hedge coordinator has not been used, the main reasons given are:
  - a preference for managing the process in house
  - trades too small to warrant a coordinator

Use of hedge coordinator



Reason for using or not using[1]



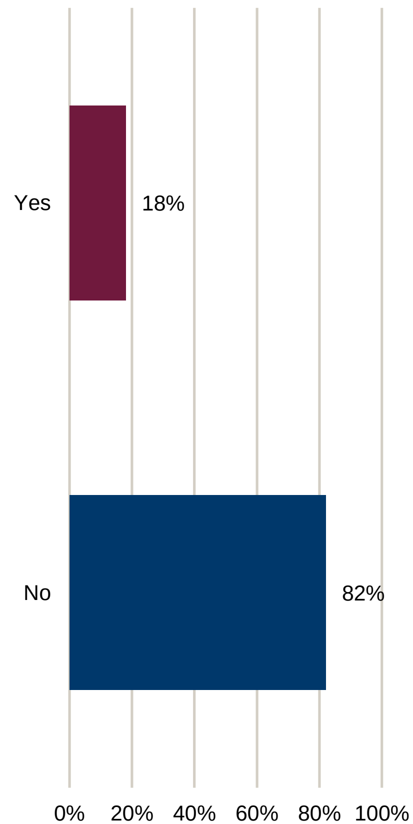
Source: Barclays. 1: Respondents could select multiple answers.

Interest rates pre-hedging

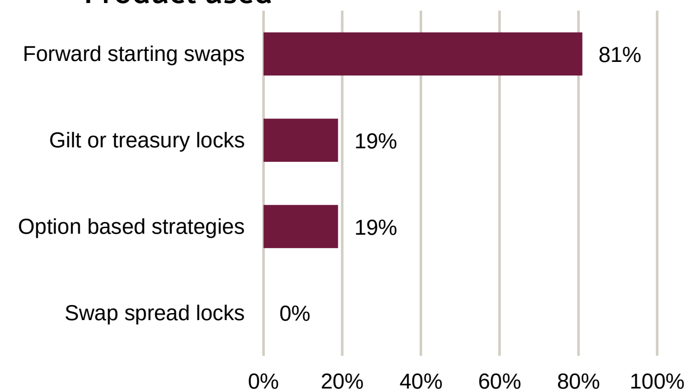
18% of companies would typically pre-hedge future expected interest rates exposures.

- 18% of companies surveyed have executed interest rates pre-hedges (for example, to pre-hedge future bond issuance or bank facility refinancing) in the past
- Where pre-hedging has been done, the primary product used is forward starting swaps, with some use of gilt or treasury locks and option-based strategies
- Where pre-hedging has not been done, the main reasons given are:
  - a lack of certainty over future debt position
  - risk not viewed as material

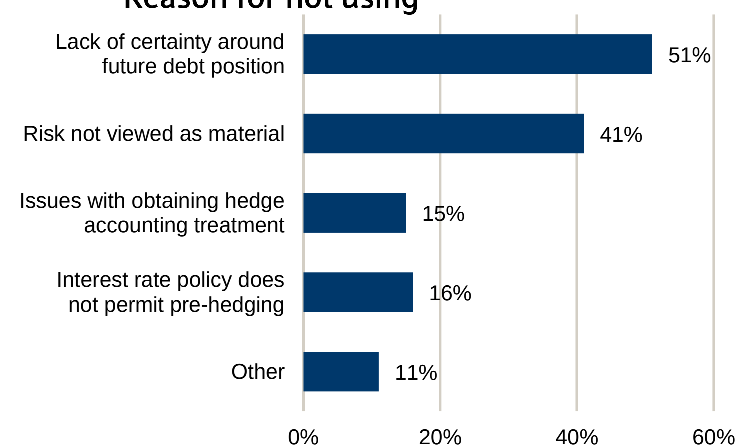
Use of pre-hedges



Product used[1]



Reason for not using[1]



Source: Barclays. 1: Respondents could select multiple answers.

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Hedge accounting

Proposed changes to hedge accounting rules under IFRS9 are expected to have a beneficial impact on corporate hedging approaches.

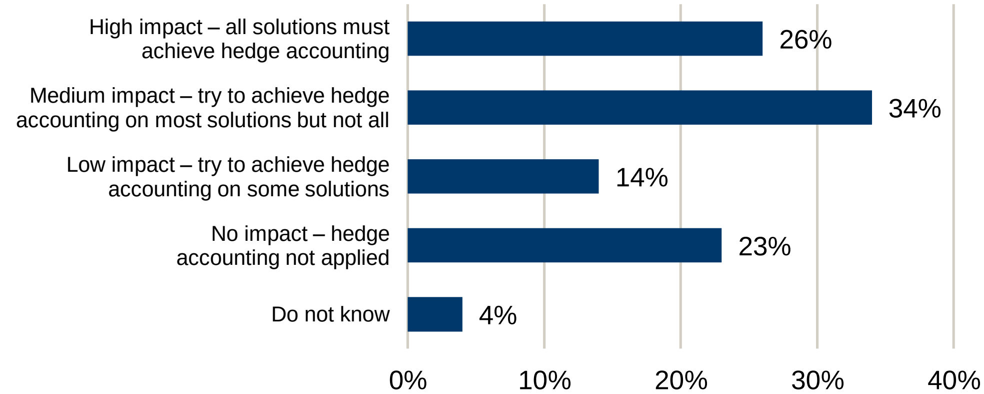
One quarter of companies surveyed state that hedge accounting has a high impact on their hedging approach

- 74% of companies have some flexibility around hedger accounting, in that not all solutions must achieve hedge accounting treatment
- Over one-third of companies state that hedge accounting has low or no impact on their hedging approach

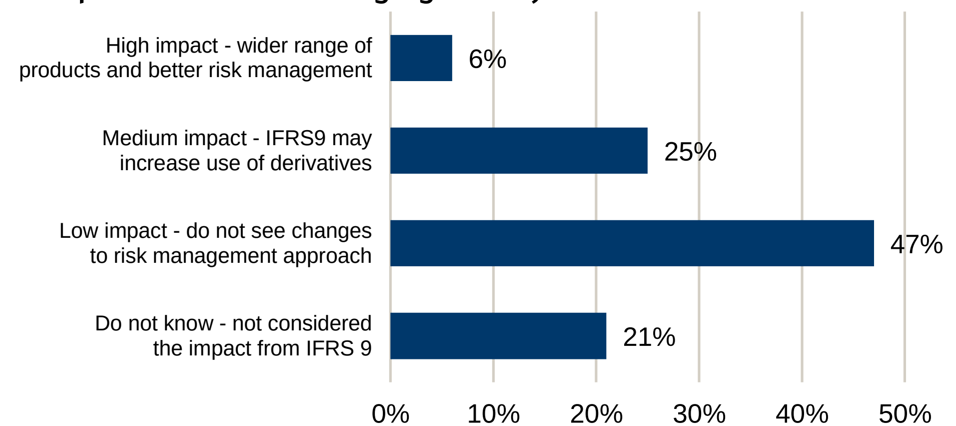
With the forthcoming IFRS9 accounting proposals, almost one-third (31%) of companies expect the changes to allow a wider range of hedging solutions, including derivatives.

One-fifth (21%) of companies have not yet considered the impact of IFRS9, suggesting that many companies are not yet prepared for these very important changes to the accounting rules.

Impact of hedge accounting on hedging activity



Impact of IFRS9 on hedging activity



Source: Barclays.

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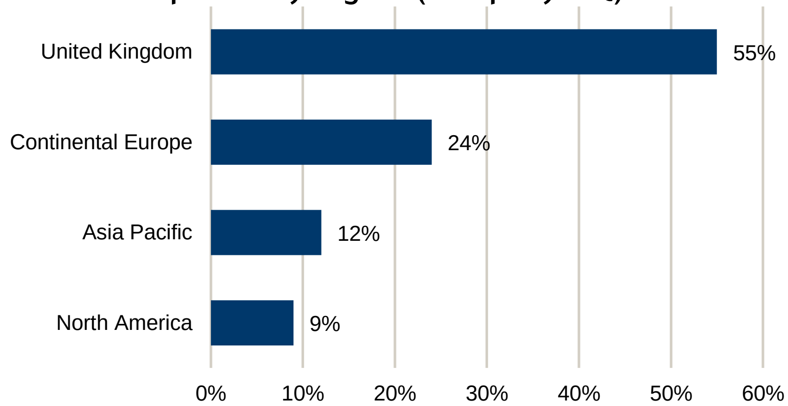
Appendix

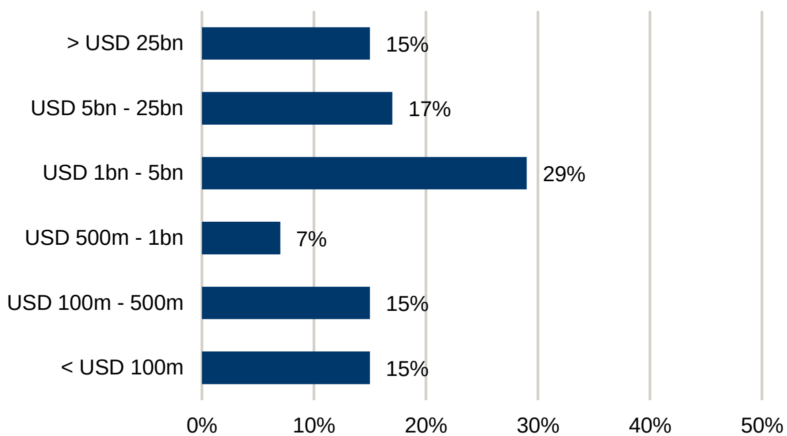
Methodology

Companies surveyed represent a wide range of regions, turnover and industries.

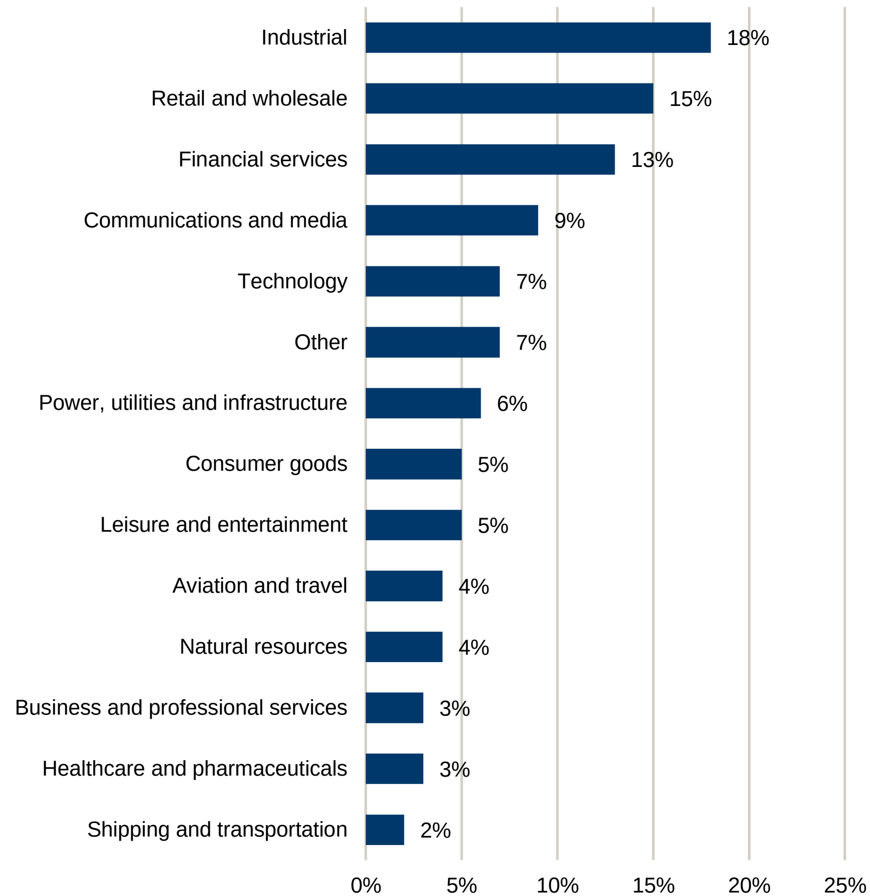
Companies by region (company HQ)



Companies by sales turnover



Companies by industry group



Source: Barclays.

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