CORPORATE FINANCE
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»France Telecom's CFO on financing €68 billion debt

»Managing Cash: The CP reversal

»Managing Risk: CF's FX Forecaster of the year results

»Manchester and Glasgow SSCs

SOMETHING TO SMILE ABOUT?

CF lists the top value-based management corporates

Gerard Ruizendaal, Group Controller, Royal Philips

CORPORATE FINANCE
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For the finance executive
March 2004
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EDITOR'S NOTE

Cash, cash and cash

Shareholder value is a mantra that gained sway many years ago. But almost as soon as the phrase had been coined, detractors began to ridicule the reality of the concept, claiming that most companies simply paid lip service to the idea of building value for their shareholders. *CF's* cover story reveals that – for some companies at least – shareholder value is more than just rhetoric.

In association with global consultants Stern Stewart, *CF* has surveyed corporates in the US, Europe and Japan on a market value-added (MVA) performance basis. MVA is a measure of excess cash generated by a company and so a positive MVA is a sign that a company has managed its cash well and that shareholders can breathe easy about how their company is being run.

But MVA is more than just a measure to see if a corporate is spending and using money wisely. In a corporate world gripped by governance fever, it is just the approach a company needs to adopt to prevent money going astray and accounting scandals.

So how do corporates define and measure shareholder value creation? *Tabitha Neville* talks to some of the top 75 companies on page 22 to find out and reveals which CFOs really know how to manage cash.

In *CF's* Managing Cash feature on page 34 we look at short-term debt, with a particular focus on commercial paper. The CP market is currently a shadow of its former self. A combination of ratings downgrades and the economic slowdown has seen the size of the US market fall to $1.3 trillion - the lowest level since 1999. So what are corporates doing to fund their short-term debt? Those who can muster the ratings are still using CP – and banks and rating agencies all claim that an upswing is just around the corner – but alternative short-term debt financing solutions are available as *Robert Pink* discovers.

On page 30, *Jason Eden* puts FX forecasters to the test in *CF's* Managing Risk feature and reveals *CF's* Forecaster of the year. How accurate are the forecasts they provide and what currencies have taken them by surprise over the last 12 months? cf

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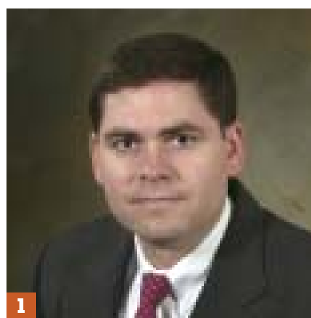

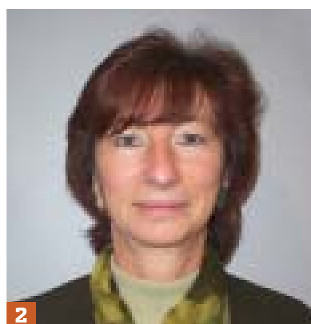

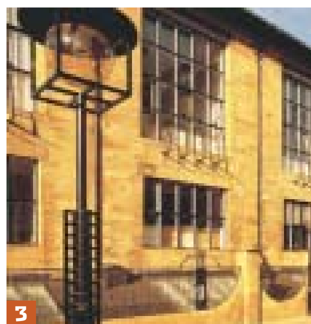

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HIGHS [& LOWS] IN CHINA

»Despite being 481 times oversubscribed by retail investors, **Shanghai Forte**'s shares only rose eight per cent on the day of its HK$1.5 billion ($192,000) IPO – a definite cool down from the 60% and 73% rises experienced by **China Green** and **Fujian Zijin Mining Industry** in their recent market debuts.

»China's largest listed lender **China Merchants Bank** reduced its planned Rmb10 billion ($1.2 billion) bond issue after shareholders, angry at the dilution of their stakes, threatened to sue. The issue would have been the largest in Chinese history but was reduced to Rmb6.5 billion. The bank will make up the difference by issuing subordinated debt.

»Ahead of its planned $1 billion listing in Hong Kong, China's first private lender **Minsheng Bank** has admitted that it falsified documents in 2000 to show shareholder approval of the bank's name change. Former director Qiu Yingxin said his signature had to have been forged as he was in police custody at the time of the supposed meeting.

»Another asset sale is planned in China, this time in the southern town of Shenzhen. The town wants to reduce its stake in about 26 state-owned companies. An asset sale in China last year attracted intense foreign interest. **Veolia Water** of France invested $390 million in Shenzhen's water utility in December.

DOUBLE YOUR MONEY

Singapore Telecommunications is punching above its weight as south-east Asia's largest phone company by more than doubling its third-quarter profits. Net income rose to S$854 ($504 million) on the back of subscriptions to its **Optus** Australian unit and favourable currency fluctuations which saw the Australian dollar rise 31% against its Singapore counterpart in 2003.

»**Singapore Air** has bounced back from the negative effects of SARS on its balance sheet by recording third-quarter profits more than double Q3 2002. Net income rose for the company rose to S$378 from S$180 a year earlier.

HIGH FASHION

» It may come as news to you - it certainly did to *CF* - that fashion branding has hit the hotel sector. Italian fashion group **Giorgio Armani** is to launch a $1 billion luxury hotel chain with Dubai developer **Amaar Properties**. With his 10 hotels and four resorts, Armani will join other fashionable hoteliers such as **Bulgari**, **Versace** and **Salvatore Ferragamo**.

NO BONUS TOO GREAT OR SMALL

»Former **Tyco** CFO Mark Swartz has admitted that a $12.5million special bonus was given to him by mistake – as was a $25 million bonus given to CEO Dennis Kozlowski – according to David Boies, a lawyer who

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Fore! Japan goes off-course

Making or breaking deals while playing a few rounds of golf before disappearing to the 19th hole has been part of corporate business for ...well forever. Sadly, if golf clubs keep disappearing as rapidly in Japan as they are currently, then businessmen there will have to go all traditional and move decision-making back into the boardroom.

Japan's golf-course industry is ridden with bankruptcy and February saw another club, **Taiyoryokka**, file for protection from creditors with consolidated debts of ¥243billion ($2.3 billion). The Japanese arm of US buyout firm **Lone Star Funds** which owns 35 golf courses, or **Goldman Sachs**, the biggest foreign investor in Japanese golf courses are seen as likely contenders to acquire the company.

Japan suffered 90 golf course bankruptcies in 2003 with debts of ¥2.02 trillion. In 2002, 109 course operators failed with debts of ¥2.19 trillion.

»Japanese bank **Shinsei** was allowed to list on the TSE despite last minute opposition from the Democratic Party of Japan, which sought to delay the IPO because of a pending lawsuit that could cost the bank billions of yen. The IPO went on to be the biggest listing by a Japanese company since **NTT DoCoMo's** $18 billion listing in 1998. Shinsei is the first bank in Japanese history to have been relisted on an international capital market after collapsing and being revived by new owners.

Japan's government isn't thrilled that the bank it bailed is now owned by a consortium headquartered offshore in The Netherlands which allows it to avoid capital gains tax on half of its 67% stake that it sold at the time of the listing. The Ministry of Finance is in talks with the Dutch government to add a clause to their tax treaty allowing it to charge capital gains tax on share sales in banks that have received public funds.

conducted an internal investigation into Tyco. In court it was a different story. Swartz claimed the $100 million paid in bonuses was early payment of annual bonuses that Kozlowski had told him had been approved by board member Phil Hampton (deceased). Six former Tyco directors – all very much alive – say they never approved them.

»The butterfly-effect of corporate scandals has now made its way to the corridors of the big four accountancy firms. A survey has revealed the firms are quietly divesting themselves of their riskiest corporate clients. The prominence of smaller companies in the ranks of the culled corporates from the portfolio's suggests that they may be more willing to take on risk when the audit fees are far larger.

Oops, silly us

CF would like to apologise to Neil and Neal. You really do look nothing alike:

Neil Preston, company secretary, Punch Taverns

Neal Neilinger, Dresdner Kleinwort Wasserstein

AFRICA

The South African government has announced an easing of its exchange controls, which will allow foreign firms to access its stock and bond markets. The JSE has been hit by falling trading volumes so foreign firms will soon be allowed to list on South African capital markets to raise debt and equity finance on the JSE Securities Exchange and the Bond Exchange.

»The Ghanaian parliament has approved **AngloGold's** $1.55 billion all-share takeover offer for **Ashanti Goldfields** after the opposition boycotted the vote, saying the deal will reduce the government's stake below the 10% level set by legislation. Ashanti's board approved the merger despite receiving an improved offer of a €1.6 billion share swap from smaller South African mining group **Randgold**.

»South African oil and gas group **Sasol** and Malaysia's **Petronas** have agreed a merger between Sasol's Liquid Fuels Business and **Engen**, 80% owned by Petronas. The merger will be a joint venture, with each company holding a 37.5% stake. The remaining 25% will be held by black partners - as required under South Africa's Black Economic Empowerment rules. This includes **Worldwide African Investment Holdings**, which owns 20% of Engen, and former shareholders of **Exel**, a liquid fuels company that merged with Sasol in December 2004.

Top Telecoms Groups

Rank	Company	Home Country	Mobile Subscribers (million)
1	China Mobile	China	153.6
2	Vodafone	UK	118.9
3	China Unicom	China	86.6
4	Cingular/AT&T Wireless	US	67.1
5	Deutsche Telekom	Germany	65.8
6	NTT DoCoMo	Japan	50.8
7	France Telecom	France	41.9
8	America Movil	Mexico	36.7
9	Telefonica	Spain	29.9
10	Verizon	US	28.8

Source: FT

What's happened to the telecoms sector?

A month ago the telecoms sector was bobbing along quite nicely, then bam! All hell breaks loose.

First up was the bustling for position in the **AT&T Wireless** deal. **Cingular Wireless** and **Vodafone** both made plays for the company, but Cingular snatched AT&T last-minute with a bid for $41 billion – one of the largest cash transactions in history – making it the fourth largest telecoms group in the world (see box).

Vodafone claims it was prudent to walk away from the auction but rumours abound of its executives being in bed asleep when the deal was struck and also that loose tongues in the Vodafone camp blasted its offer from the water (it is alleged Vodafone told reporters that the Vodafone board were going to approve a bid of $14.50 per share; Cingular got hold of this information and hey presto a bid of $15 per share). What's that expression? Careless talk costs acquisition opportunities.

»February also saw Belgian incumbent telecoms company **Belgacom** put the finishing touches to its IPO. The €3.5 billion ($4.4 billion) share sale will be the largest IPO in Europe in the last three years.

»**France Telecom** got round to launching an offer to buyout the remaining 29.4% of **Wanadoo**, its directories and internet services division. The €3.9 billion offer is awaiting Wanadoo's approval.

»**XO Communications**, which emerged from Chapter 11 a year ago, unveiled plans to acquire other distressed telecoms. The company has just won an auction for the bulk of **Allegiane Telecom's** assets for $628 million.

»**China Telecom** may raise as much as $3 billion through a share placing to fund the acquisition of 11 regional telecom networks from its state-owned parent company, which would add 45 million users to its subscriber base.

Strike while high yield's hot

»Issue volume hit €16.6 billion in 2003
»Move from refinancing activity to find M&A

The high yield market in Europe was the turnaround story of 2003. New issue volume hit a record high of €16.3 billion after a miserable two years. What can issuers expect this year?

Standard & Poor's says that prospects of a cyclical recovery, a continued accommodative monetary policy stance, declining default rates, and a slowdown in credit quality deterioration in the European high yield market will mean that corporates should have strong conditions in which to issue in – though S&P also notes that corporate downgrades continue to be substantially higher than upgrades.

"Conditions remain favourable in Europe," says Diane Vazza, managing director in global fixed income research at S&P in New York. "Monetary policy is really helping to keep it that way." Stephane Tremelot, head of credit syndicate at BNP Paribas in London, agrees that "slow[er than expected] economic growth in the eurozone and the dollar/euro exchange rate mean that it is unlikely that the ECB will raise rates in the short term. That means that there is an opportunity for issuers to benefit from issuing bonds with low yields."

Even if rates do rise, it doesn't necessarily spell an end to issuance, according to Nicholas Coates, head of high yield at RBS in London. "Some issuers may make opportunistic moves to do deals before rate rises take place but issuers can always use the swap market to get comparatively lower floating rates."

While spreads in the US high yield market have widened by around 8bp since the beginning of the year, in Europe they have continued to tighten and are around 38bp tighter than at the end of 2002, according to Tremelot. Indeed, the average absolute yield for European issues remains lower in Europe at 7.44% than in the US at 7.87%.

Some market observers fear that Europe is about to succumb to the problems troubling the US market, where fund flows information provider AMG Data Services has reported net outflows from high yield funds in the US for three of the four weeks to February 25. While these outflows are specific – and thus far isolated – to US funds, their impact is more widely felt: many of those funds also invest in the European market; and trends in the US high yield market frequently pre-empt those in Europe.

Nevertheless, S&P's Vazza – and most market observers – say that this is just a hiccup. "Investor demand is still there but there has been a realisation that corporate spreads have tightened too fast compared to credit quality and that there was a need to set that right." Coates adds: "Whilst the European high yield market has softened over the past month, we believe this to be a temporary phenomenon: a correction to a bullish market. The long-term trend is for increased liquidity in Europe and demand will remain strong as funds continue to flow into the market." More bullish commentators say that the softening of the market has resulted from investors selling bonds in order to have cash to respond to the expected deluge of new issuance expected.

Either way, no-one expects the high yield markets in Europe to flounder this year. Issuance YTD has been limited – around €2 billion from 10 deals compared to $25 billion from around 100 deals in the US – but BNP Paribas' Tremelot says that this is common for this period of the year. "Unlike the high grade world January and February are quiet months as issuers and banks prepare new transactions."

While it is impossible to know if we are at the bottom of the credit cycle, all the indicators show that the economy is improving, credit quality is improving, and investor demand isn't about to collapse.

And while all these factors may be pulling issuers to the high yield market, the long-term structural trend of reduced bank lending – not least because of Basel II – is also pushing issuers toward it.

> **"European corporates increasingly view the high yield product as a mainstream financing tool."**
> Nicholas Coates, RBS

"Banks have become much more focused on the risk adjusted returns of their credit provision and are often less resistant than they have been in the past to corporates diversifying their sources of funding away from the bank market," says RBS's Coates. "That is a significant change."

Who's issuing?

The high yield market has traditionally been driven by three sources of issuance – leveraged buyouts (LBO), telecom, media and technology (TMT) and general corporate issuance. "For the first time these three components of the primary high yield market in Europe will produce deals simultaneously this year. That means that we can expect a strong level of issuance," says Coates.

LBO issuance is expected to provide a quarter of the market in 2004 while TMT issuance should match last year issuance of almost €6 billion. But the key to the potential market growth is corporate issuance.

One of the main reasons for the growth of the European high yield market in 2003 was issuance from fallen angels – issuers that have fallen to speculative (rated BB+ and below by S&P and Ba1 by Moody's) from investment grade (BBB- and above by S&P and Baa3 by Moody's). Of the total €16.3 billion raised in Europe, fallen angels accounted for

€6.4 billion or 40%. S&P points out that that is a 25% increase on 2002 figures. As a direct consequence of increased fallen angel issuance the average deal size in the European high yield market increased from €251 million in 2002 to €286 million in 2003.

Investors have been understandably eager to buy paper from such issuers. "HeidelbergCement came to the market at a time when investors were looking for a way to get a better yield on their investments," says Christian Kammann, group treasurer at the company. "HeidelbergCement also strongly pointed out the commitment to go back to investment grade. The deal brought by us was the largest European high yield deal then and in many ways set a market standard."

Issuance from fallen angels has not only swollen the market's overall size it has coaxed other issuers into the market. "Issuance from high quality borrowers such as HeidelbergCement and Vivendi in 2003 helped to 'destigmatise' the market and it's now a lot easier for CFOs to justify using the market to their boards," says Coates. "The corporate sector will continue to be buoyant as European corporates increasingly view the high yield product as a mainstream financing tool."

The use of that financing is expected to change, says S&P's Vazza. "The focus is shifting from refinancing to capital spending. It can be expected that the European market will follow the US in the move away from refinancing activity to fund expenditure and M&A activity." **LN**

Europe – Structure changes benefit issuers

The European high yield market has traditionally been dominated by 10-year bonds with a five-year non-call. If issuers wanted to redeem before that five-year call they would have to tender for the bonds – a costly process most were eager to avoid. The rationale was that a five-year call gave issuers reasonable flexibility to get their finances in order and work their way back to investment grade while investors would not get unduly punished by companies eager to refinance debt once their credit quality had improved.

Issuers are now in pole position, with vastly more demand than new issue supply. As a consequence, issuers have been able to get better terms from investors. Instead of 10-year deals, issuers have begun to bring seven- or eight-year deals. Crucially, the calls on these bonds are also shorter – giving finance executives' greater flexibility to refinance should their financial and rating position improve.

There has been a move toward seven-year bonds with a four-year non-call at half-coupon meaning that investors get half the coupon rate if the bonds are called. A number of issues have also come with three-year non-calls at full coupon. Issuers might have to pay a bit more to get this even shorter call, but it offers them an enormous flexibility advantage over a traditional 10 year non-call five bond. Understandably, investors are unhappy with the changes but concede that they are a function of an efficient market.

S&P notes the near-term outlook for European high yield is benign "with the outlook and CreditWatch distribution indicating an improvement in credit quality relative to a year ago". Only 25% of speculative rated issuers currently have a negative bias, compared to 30% a year earlier.

Timetable of a high yield bond

High yield bonds take longer to come to market than investment grade bonds for a number of reasons. Chief among these is that issuers are frequently unrated before they issue. Meanwhile, the documentation and offering circular must be put together by the issuer's investment bank.

Choosing your market is a key decision says Christian Kammann, group treasurer at HeidelbergCement. He says issuers should weigh up both the cost and investor familiarity benefits. "The European investor base was more familiar to the HeidelbergCement credit." He adds that the complex legal environment in the US market dissuaded the company from issuing there. Simply printing a "144A issue [allowing the sale of a non-US market bond to qualified US investors] makes the due diligence process more extensive". Although it allows issuers to benefit from the price tension that reaching a broader investor base creates.

A further time consuming element of high yield bonds is that the covenant package offered to investors is frequently more complex than with investment grade issues. High yield issuers have a higher risk of default and therefore investors require greater protection, as Kammann explains. "High yield investors are more focused on covenants and protecting or keeping the cash flow in the company for debt reduction that results in a much more detailed indenture."

The less developed nature of the market also means that some covenant packages become a matter of negotiation with investors rather than simply being drafted by the issuer. "Familiarity with the high-yield style of documentation and cross-checking with operational/strategic needs of the issuer group are vital," Kammann says.

From the awarding of the mandate to completion, a high yield issue should take around two months.

Deal of the month: Yamanouchi Pharmaceutical

Pharma's strength in numbers

DEAL AT A GLANCE

» $8 billion merger of Japanese pharmas
» Pharma consolidation in Japan set to rise

Pharmaceutical companies Yamanouchi and Fujisawa agreed an $8 billion merger creating Japan's second largest pharma entity in February.

Yamanouchi and Fujisawa Pharmaceuticals Japan's third- and fifth-ranked drug makers respectively, aim to reach an agreement by March 2004 and integrate operations by early 2005.

Enhancing R&D and marketing opportunities are the principal factors behind the merger which will see each Fujisawa share exchanged for 0.71 Yamanouchi shares. The deal will create the 17th largest firm in the global market. "From a business point of view most people have said it's a very good combination, as well as from a geographic point of view," said a banking source close to the deal.

Japan is the second largest pharmaceutical market after the US, with sales of around $52 billion in 2002. Yet Japanese pharmas have never been viewed as global players. Yamanouchi , for example, has been struggling in the United States. A core reason for this, is R&D spend. The ratio of R&D to total sales in 2002 was 12.8% for Japan's pharmaceuticals, compared to an average of over 17% for Western counterparts. And by limiting the influence of foreign competition in Japan, government protection has further limited R&D investment to below that of foreign rivals. The merger will, analysts hope, address the imbalance. (The acquisition of Pfizer by Pharmacia in 2002 created an R&D budget worth $6.5 billion. The combined R&D budget for Yamanouchi and Fujisawa will be ¥150 billion ($1.3 billion)).

"The merger should improve the competitiveness of the new entity," comments Shinsuke Tanimoto, an analyst for Moody's Japan. "The increase in the size of the business will, on a global basis, broaden sales coverage and strengthen R&D capabilities." It may also spark off more sector consolidation.

Yamanouchi and Fujisawa have both admitted that they needed to merge to fend off overseas competition in the world's second-largest drugs market. And with the government actively promoting foreign share-ownership and competition in the market and western companies such as Merck, GSK and Pfizer expanding their marketing in Japan, it is likely other Japanese companies will follow in its footsteps. Tanimoto agrees: "The merger of Yamanouchi and Fujisawa could affect the balance of the market competitiveness in the top tier players and might accelerate market reorganisation."

Japan's government is also in the mood for change. It is has publicly stated that it wants to see consolidation in the industry. It is slashing both the number of drugs which can be sold only by prescription, and the amount paid for drugs through the national health system, both changes which weaken domestic drug makers in their battle with foreign drug companies.

Yamanouchi's president, Toichi Takenaka, will become chief executive of the new company, which will retain his company's name. Fujisawa's president, Hatsuo Aoki, will become chairman.

Morgan Stanley Japan advised Yamanouchi; Lehman Brothers Japan advised Fujisawa. **RP**

Global Pharmaceutical sales by Region, 2002 (US$ bn)

World Audited Market	Sales	Global Sales %	Growth %
North America	203.6	51	12
Europe (EU)	90.6	22	8
Rest of Europe	11.3	3	9
Japan	46.9	12	1
Asia, Africa and Australia	31.6	8	11
Latin America	16.5	4	-10
Total	**400.6**	**100**	**8**

Source: IMS World Review 2003 and IMS Consulting

COMPANY INFO

Yamanouchi is strong in ulcer and urinary treatments and is best known for Harnal, a medicine for urinary problems. It was founded in 1923; has capital ¥99,760 million; total assets ¥890,525 million; and 8,957 employees.

» Fujisawa makes the immuno-suppressant drug Prograf, and focuses on immune-related treatments. It was founded in 1930; has capital ¥38,589 million; total assets ¥508,354 million; and 8,059 employees.

» Combined sales of Yamanouchi and Fujisawa in the current financial year to March 2004 will likely reach ¥920 billion ($8.4 billion dollars).

» The two companies have ¥890 billion in combined sales, and the deal will allow them to surpass the one trillion mark. It will have the largest market share among Japanese pharmaceutical companies.

» It will be 17th in the global pharmaceutical market

» The combined company will: have an annual R&D budget in excess of ¥150 billion;have more than one trillion yen for sales; and 25% as an operating margin.

» In 1995 overseas shareholders held 17.1% of Yamanouchi stock. By 2002 the figure had risen to 44.7%. Takeda, Japan's leading pharmaceutical, has seen foreign share ownership rise from 10.1% to 29.6% in the same period.

MARKET FOCUS

Invensys restructures with £2.7 bn refinancing

» Invensys replaces £1.4 billion credit expiring 2005
» Plan reduces disposals to £250 million

Early in February UK engineering group Invensys announced a broad restructuring backed by a £2.7 billion ($5 billion) refinancing package - its third attempt in two years to create a new plan for its future.

The Invensys refinancing package includes a £450 million share placing, a £625 million high-yield bond, which later had to be scaled back in the face of investor resistance, and a £1.6 billion five-year credit facility. The new package replaces £1.4 billion of borrowing facilities due to run out by 2005.

The group has suffered financial problems almost since its inception - it was formed by the merger of BTR and Siebe five years ago. At the time of the announcement in February this year, its debts were estimated at about £1.4 billion, compared to a market capitalization of £840 million.

The refinancing package has more than a hint of opportunism in it - taking advantage of improved market conditions and investor sentiment. It is also a definite change of tack which has been ill-received (see box).

Immediately, Standards and Poor's lowered its long-term corporate credit rating to B+ from BB-, as a result of the company's expected high levels of leverage in the medium term, and its existing debt ratings to B- from B. Moody's is considering downgrading Invensys's current rating of Ba3, citing: "the impact of the changes in disposals strategy on the company's financial profile and the size and stability of the remaining business to support residual debt levels."

Fitch Ratings compares Invensys's refinancing unfavourably to those of fellow engineering groups ABB and Alstom. "Unlike ABB and Alstom, Invensys is not subject to material external factors, which act as a drain on financial services, other than those inherent in the industry. In the case of Invensys, the group's problems have arisen from ongoing operation and financial issues, notably poor working capital management. Invensys is proposing to issue a placing and open offer in contrast to the rights issues carried out by ABB and Alstom [which] is indicative of the degree of uncertainty and lack of market confidence as to whether or not the group will gain the support required from its existing shareholders.".

Victoria Scarth, SVP corporate communications at Invensys, refutes the accusation of a lack of market confidence in the company, pointing to the success of the refinancing. "The success proves the company is doing what is needed and that investors have confidence in the company. We've had a lot of legacy liabilities, product and environmental issues, litigation, that have been obscuring our operating cash flow. Adrian [Hennah, CFO] has done a forensic job of isolating the liabilities and addressing issues from our long conglomerate history.

"We've set up an escrow account of £560 million ring-fenced to deal with the liabilities. That caps the value of the liabilities for the market and we report on that quarterly, which makes our work on the working capital more transparent. Our commentators will see a cleaner flow through profit to cash. These changes have established confidence and that's why investors have supported the refinancing. We didn't ask for equity before because the business was complex. Things weren't clear but a lot of work has been done in two years to improve this."

There is no question about the deal's success for Invensys's advisors. The challenging nature of the deal and the fact that the banks underwriting the deal took on so much risk means that the bankers, lawyers and other advisors will earn up to £108 million in fees – 12% of the company's market value. Deutsche Bank was lead underwriter with Morgan Stanley and Cazenove also underwriting the equity placing. Morgan Stanley, Cazenove and Tricorn Partners advised.

Nick Wiles, co-head of corporate finance at Cazenove, one of Invensys's advisors, says: "It was a particularly challenging deal because of the use of the debt market and the equity market simultaneously. There was intense pressure to coordinate and execute at the same time, but it was a real moment to take in the market." **MW**

PENSIONS UPSET

In 2001, CEO Rick Haythornthwaite told investors that he planned to cut the size of the company by a third. Last year he named more divisions to be sold and in November 2003, he revealed the company expected to make £1.8 billion in disposals. But the company's restructuring plans reveal this figure has been reduced to the paltry sum of £250 million. This aspect of the restructuring has been badly received by Invensys's pension scheme trustees. When the company planned to make £1.8 billion in disposals in November last year, it pledged to put 15% of any proceeds over £1 billion into the pension fund. With disposals set at £250 million, Invensys isn't saying whether any of the £2.7 billion of refinancing will go into the plan. The company's pension plan has a deficit of £885 million. It has 100,000 members, only 15% of which are current employees.

Global consolidation efforts set to rise

» Increased earnings encourage acquisitions
» 389 deals totalling $21.5 billion in tech sector YTD

In a scene akin to the last dance at a disco with everyone scrambling to find a partner, corporates can be seen scanning the landscape for acquisition opportunities hoping to cherry pick victims before the M&A spree really kicks off.

Year-to-date more than $350 billion of proposed acquisitions have been announced - more than three times the amount in the same period for 2003. Some of this can be accounted for by deals that have been moving through the investment banking pipeline for some time and are finally coming to a close, but stock market rallies, low interest rates and renewed optimism in the deal-making environment are all helping to push corporates to make M&A decisions.

"Companies have been focused on their balance sheets and earnings for the last few years, but now that earnings are growing again and their internal problems are fixed, they are looking to grow and the best way to grow and the best way to do that quickly is through M&A," says Richard Morgner, head of mergers and acquisitions at investment banking boutique Chanin Capital Partners. It seems the boards of technology and telecoms firms as well as of financial institutions are of the same mind. The tech sector has seen 389 deals totalling $21.5 billion YTD, while in the finance sector, there have been 132 deals totalling $111.6 billion YTD.

Technology

Within the tech sector, the semiconductor industry has seen a spate of acquisitions such as Singapore state-controlled ST Assembly Test Services (Stats) purchase of US-based ChipPAC for $1.6 billion in February.

"The whole semiconductor manufacturing side of the business is getting to where the investments to do manufacturing are so high, you've just got to have a big company to play in the game," says industry observer Jim Mulady, publisher of The Final Test Reporter, a semiconductor industry newsletter. Consolidation in the semiconductor manufacturing industry is necessary to contain costs and increase efficiency, he adds.

Acquisitions in the semiconductor sector are following an increasing trend towards outsourcing by integrated device manufacturers (IDMs) - large chip companies that have traditionally designed, manufactured, tested and assembled semiconductors - who now need to streamline their operations to help their cost competitiveness.

A recent report from Morgan Stanley's Global Semiconductor Research Team says that by 2010, the semiconductor industry will grow to $360 billion with 34% of the industry driven by outsourcing revenue.

"Streamlining can be done easily through outsourcing and assembly and testing are good areas to outsource because they require less disclosure of proprietary information," says Chris Hsieh, regional head of Asian technology research at ING in Taipei.

Outside of the semiconductor industry, there have been several other major acquisitions, such as US Internet systems provider Juniper Networks's purchase of US network security provider Netscreen for $3.6 billion. The deal involves 1,404 shares of stock for each of Netscreen's shares.

Michael Cohen, director of research for Pacific American Securities, says the Juniper acquisition is a perfect example of how some larger tech companies are willing to use their shares to do deals. As such, he predicts "there will be more acquisitions to come since many tech stocks surged last year."

Financial Institutions

Following the announced $58 billion merger of JPMorgan Chase and BankOne, and Bank of America's acquisition of FleetBoston Financial for $43 billion, the financial institutions sector is rife with speculation of more M&A activity to come.

So begins the consolidation

In a recent pan-European study, Credit Suisse analysts said that with economies recovering, capital building up and questions over future earnings growth "some management teams may now feel under pressure to turn to acquisitions as a way of boosting earnings".

Co-CEO of Credit Suisse Oswald Grubel has said he sees opportunities for acquisition-led expansion in Germany and MBNA Europe CEO General Charles Krulak is expecting further consolidation in the credit card business, following his company's purchase of the credit card books of UK banks Abbey and Alliance & Leicester (A&L).

"Over a period of time there will be banks who issue credit cards right now who say maybe the idea would be to do something like Abbey and A&L have done. I think you will see consolidation.

"The questions regarding Egg [which has been put up for auction by Prudential] are an example of that, where you have a very nice business that is owned by a shareholder who is saying maybe someone else can do this," adds Krulak.

Meanwhile, BNP Paribas CEO Baudouin Prot says he is "actively searching" for acquisitions to follow the pattern set by the €9 billion of deals done by the bank since the merger of BNP and Paribas in 1999. **MW**

Indian government paves way for privatisation

» Biggest off-loading of shares undertaken
» Privatisation to regenerate state-owned industry
» ONGC 10% stake sale

March 2004 is gearing up to be a busy month in the Indian equity markets. So much so that investors have already nicknamed it privatization month.

Privatization month will see the biggest off-loading of shares ever undertaken by the Indian government (or any government worldwide) – it will divest more than $3 billion of state-owned stock. If the part-privatization is fully subscribed it will become the largest equity placement in India's capital market history.

The equity sale forms part of a government initiative designed to regenerate a percentage of the country's hitherto traditionally state-owned and controlled industries. By selling a proportion of their share holdings, expanding the capital market base and increasing liquidity, the Indian Government hopes to attract foreign investment and intellectual expertise.

"The government is looking to establish widespread ownership, and eventually, a total divestment in companies that it perceives as being in non-core areas, i.e. sectors that are not classified as affecting national security," says Ravi Menon, director of investment banking at HSBC in Mumbai.

"This is all part of a government initiative that really kicked off in June 2003, when the IPO from Maruti began to open up the domestic equity markets to foreign institutional investors," says Yogesh Shetty, group director of commercial foreign exchange at Travelex.

The government's jewel in the crown, and a highlight of privatisation month, will be the public offering of a 10% stake in the Oil and Natural Gas Corporation (ONGC) India's largest domestic company by market capitalisation, worth an estimated $2.5 billion. The government owns 84% of ONGC at present and will retain a majority stake in the company, along with effective control after the sale is completed.

Other state-owned heavyweights hitting the markets in March include Gail, the largest gas distributor, the Bank of Maharashtra, IBP, the oil retailer, and the Dredging Corporation.

The Government has tried and failed in the past to partly privatise some of India's largest state-owned

In brief

»Nokia plans to buy out **Psion's** share in **Symbian**, in a move to consolidate its influence on the operating system used in most European smart phones. The £135.7 million deal would increase Nokia's stake from 32.2% to 63.3%, but it is facing strong opposition from Psion's largest shareholder who says an IPO of Symbian should be considered instead.

»Juniper Networks is to acquire network-security software maker **NetScreen Technologies** for $3.6 billion in stock. Juniper has been buoyed by a recovery in the telecoms sector. It reported fourth quarter net income of $14.7 million up from $8.5 million.

»Singapore-based **ST Assembly Test Services** made a $1.6 billion bid for Silicon Valley's **ChiPAC**. The deal will create the third-largest company in the chip assembly and test services "back-end" service provider market behind Amkor technologies and Advanced Semiconductor Engineering.

»Diners Club Malaysia announced the first asset-backed securitization for its charge card receivables in Malaysia with the issuance of **Domayne Asset Corporation Bhd's** (DACB) RM132 million ($34.7 million) Medium Term Notes of 3.5 years tenure. Diners Club Malaysia will sell its charge card receivables on a revolving basis to DACB which will, in turn, raise the financing by declaring a trust over these receivables and issuing MTNs. This is the first securitization deal of its kind in Malaysia.

»Russia's sixth-largest oil company, **OAO Tatneft**, won approval from the Turkish government to buy a majority of oil refiner **Tupras** for $1.3 billion. Tupras controls 87% of Turkey's refining market.

»Enersur, the Peruvian-based subsidiary of Belgian energy company Tractebel, won a 30-year concession from the Peruvian government for the 130MW Yuncan hydroelectric project. Enersur bid $53 million. Norway's state power company **Statkraft** and the US-based **PSEG** declined to take part in the bid.

»Financing for the largest pipeline project in history – the $3.65 billion **Baku-Tbilisi-Cayhan** – was completed in February. The financing for the project which spans three jurisdictions and over 1700 km, needed 17,000 signatures to be finalised. The project is being developed to provide a primary export route for oil produced off-shore Azerbaijan.

»Suez-Tractebel of Belgium and **Mimag** of

Follow-ons by Indian Issuers 01/01/00 - 20/02/04

	Amt. m (US$)	Iss.
2000 1st Quarter	499.49	4
2000 2nd Quarter	108.75	1
2000 3rd Quarter	86.38	2
2000 4th Quarter	130.85	1
2001 1st Quarter	0.00	0
2001 2nd Quarter	294.69	2
2001 3rd Quarter	172.50	1
2001 4th Quarter	0.00	0
2002 1st Quarter	0.00	0
2002 2nd Quarter	0.00	0
2002 3rd Quarter	50.00	1
2003 1st Quarter	0.00	0
2003 2nd Quarter	0.00	0
2003 3rd Quarter	346.25	2
2003 4th Quarter	87.97	2
2004 1st Quarter	0.00	0

SOURCE: DEALOGIC

Indian IPO Quarterly Breakdown 01/01/00 - 20/02/04

	Amt. m (US$)	Iss.
2000 1st Quarter	29.78	3
2000 2nd Quarter	66.34	3
2000 3rd Quarter	22.37	1
2000 4th Quarter	50.85	6
2001 1st Quarter	44.83	5
2001 3rd Quarter	0.96	1
2002 1st Quarter	205.72	2
2002 2nd Quarter	42.85	1
2002 3rd Quarter	59.19	1
2002 4th Quarter	92.51	2
2003 1st Quarter	9.91	1
2003 2nd Quarter	213.66	1
2003 3rd Quarter	63.15	4
2003 4th Quarter	72.38	2
2004 1st Quarter	150.18	3

SOURCE: DEALOGIC

companies – in February 2002 it privatised VNSL (Videsh Sanchar Nigam Limited), one of India's largest ISP providers, with only limited success. Menon believes the government's timing is better this time around.

India is emerging as one of the fastest growing economies in the world, propelled by rising consumption, and the record inflow of foreign investment. GDP is expected to hit 7.5% in the fiscal year to March. This figure is way above anything the Eurozone or America can hope to achieve. As for the timing of the sell-offs, it could not be better: the equity capital markets have experienced an unprecedented bull run in the last six months (they saw a 60% rise in 2003). "It's a great time for the government to act. These factors ensure that investors are subscribing, and the government gets a great price for its divested stock," says Menon.

The performance of one of the first deals to hit the markets certainly bodes well. Petrochemical company IPCL's shares have soared 97.8% over the last 12 months and the offering was healthily oversubscribed by 10% as investors flocked to what they see as stable companies with under-valuation mandates. "Many of these companies are extremely healthy and are blue-chip in their own right," says Menon. **JE**

In brief

Turkey, closed a $475 million financing for the Baymina power project near Ankara, Turkey.

»**Fiat**'s asset sale program was completed in February with the sale of 70% of **Fiat Engineering** to privately held **Maire Holding** for €80.5 million ($101.7 million). In 2003 the company sold insurance company **Toro Assicurazioni** to publisher **De Agostini** for €2.4 billion and **Fiat Avio** for €1.4 billion to the **Carlyle Group** and **Finmeccanica**.

»Singapore saw its largest IPO of the year in February. **UTAC**'s offer was 32.5 times oversubscribed. The semiconductor test and assembly company raised S$182.6 million ($107 million).

»Las Vegas-based **Boyd Gaming** is to buy rival **Coast Casinos** for $1.3 billion in cash, stock and debt.

»Brazil's two largest airlines **Varig** and **Tam** have decided against merging. They spent a year negotiating, unsuccessfully, to deal with a complex ownership structure, large debt and legal challenges. They will instead form a small joint venture and expand their code-sharing arrangement.

»The Mexican government has approved Spanish bank **BBVA**'s $4.2 billion offer to buy the remaining 40.6% of Mexico's **BBVA Bancomer** that it does not own. This will take BBVA Bancomer out of the Mexico City stock market, where it is the largest financial services stock accounting for 85% of the financial services index. This deal, in combination with the recent buyout of Mexican cement firm **Apasco** by **Swiss Holcim**, will reduce the liquidity of the Mexican stock exchange by 10%, according to analysis by UBS Warburg.

»**PwC** expects the volume of IPOs in China to grow by 70% in 2004. The firm believes 100 companies will go public in Hong Kong in 2004, raising approximately HK$100 billion ($12.9 billion) compared to HK$59 billion raised in 2003. IPOs by Chinese companies could account for 80% of funds raised in Hong Kong, with large listings expected from China Construction Bank and Minsheng Bank.

»**Aventis**, the Franco-German pharmaceutical company fending off a €46 billion bid from **Sanofi-Synthelabo**, has gone on the offensive. It has announced plans to buy-back between €2 to3 billion of shares, and dispose of non-strategic products in an effort to streamline the business. Aventis's chairman, Igor Landau, says that Sanofi's €46 billion offer had fundamentally undervalued the group.

Mover of the month: John Cavanaugh, Goodyear

'New' assistant treasurer post for Cavanaugh

When *CF* spoke to John Cavanaugh in February, it was surprised to learn that two weeks into his newly-created role of assistant treasurer for Goodyear Tire Company, he didn't have an office or a phone.

Cavanaugh, 33, a former US marine, joined Goodyear in July 2003 as director of financial strategy before being promoted to assistant treasurer by Goodyear's treasurer Darren Wells, who recognised there was a need for a skilled and experienced assistant treasurer to assist with the the restructuring.

The past two years have been difficult for the tyre company. It has lost $1.3 billion in revenue and faced considerable difficulty cutting costs because of protracted trade union talks in the US. Things picked up in April 2003, when a three-year $1 billion cost-cutting deal was agreed on with the unions and there was further good news in September when it achieved the partial restructuring of its corporate debt with the replacement of a largely unsecured portion of $2.94 billion in financing with $3.3 billion in secured credit lines. Reports of accounting errors, uncovered in October worth $84.7 million since 1998, and an SEC investigation, set it back.

"The move to assistant treasurer is at the forefront of Goodyear's refinancing plans," says Cavanaugh. There was an assistant treasurer at Goodyear 10 years ago, but the position was deemed surplus to necessity as the company's fortunes grew. "As the company ran in to problems the need to reorganise the treasury to deal with the complexities it faced became more important." So how does his role differ to that of director of financial strategy?

More responsibility, says Cavanaugh. "As director of financial strategy, I was responsible for domestic and international financing, foreign currency, and to some degree corporate reporting. Now I manage cash management and the banking and rating agency relationships too." Not an easy task. Goodyear's plan to operate a $650 million credit line has prompted S&P to downgrade its existing bank loan and notes from BB- to B+. Fitch also downgraded Goodyear's senior unsecured rating to CCC+ from B, affecting around $5 billion worth of debt.

"Obviously, coming from Kmart, which is an investment grade company, the finances at Goodyear will be more of a challenge. In an investment grade company, there is much less reliance on the banks to provide liquidity and cash. You can access the CP markets or put up an asset-backed receivables programme, for example. At a sub-investment grade company you are reliant on the banks for a liquidity funding line to draw on."

Cavanaugh's immediate concern is to help turn the company round, a process that will take some years, he says, but that's not to say he's not looking ahead to Goodyear's rejuvenation. "After we have stabilised the company, the next big challenge is to manage cash globally. Historically, Goodyear has been decentralised but we plan to put a system in place which will allow us to move cash across borders more easily and that provides capital when it is needed. We would also like to be able to manage the costs of managing the cash."

The 'we' here is Cavanaugh and Darren Wells, Goodyear's treasurer and a past colleague of Cavanaugh's. The pair worked together at Visteon - the principal supplier of parts to Ford and from where both joined Goodyear. Wells joined Goodyear in the summer of 2002 as vice-president and treasurer and obviously rates Cavanaugh's experience enough to bring him on board.

"I have worked with talented people, and I very much enjoyed working for Darren. When he left we kept in touch. The move to Goodyear was an obvious one. I was the director of capital markets at Visteon, and so was familiar with the refinancing procedure before I joined," explains Cavanaugh. "As such, I was able to come in to the company and help right away." **RP**

"The finances at Goodyear will be a challenge. In an investment grade company there is much less reliance on the banks to provide liquidity and cash."

AT 33, CAVANAUGH IS CLIMBING QUICKLY

John Cavanaugh spent five years in the US Marine Corps, before opting for a career change. "Smartening up," he calls it. An MBA stimulated his interest in finance and a CFA qualification followed before a position at Kmart. "I enjoy the financial engineering aspect to treasury, I enjoy the relationships you develop with lenders and optimizing the capital structure of the company."

»Feb 2004: appointed assistant treasurer at Goodyear
»2003 – Jan 2004: director of financial strategy at Goodyear
»2000 – 2003: director of capital markets at Visteon
»1998 – 2000: involved in financial analysis and treasury at Kmart

Crudele strikes a chord with Gibson Guitars

Rock stars can be quite hard to find in the world of corporate finance, although we did once speak to the accountant for Pink Floyd. And *CF* isn't about to deliver a rock profile but it has found a strong link to the world of pop with Anthony Crudele, the recently appointed CFO of Gibson Guitar.

CF: *So what's it like to be a finance man in the entertainment industry?*
AC: Although we are an entertainment company, our core business unit centres on the manufacturing of fretted instruments.

CF: *But manufacturing Gibson guitars is surely more sexy than traditional manufacturing, isn't it?*
AC: Technology is a great change agent and our CEO, [Henry Juszkiewicz], has utilized technology to improve our business processes in manufacturing as well as to bring the power of the Gibson brand to bear in other areas and parts of the world. In just the last few years, we have expanded the Gibson name into web based retail, bricks and mortar retail, artist showcases and most recently in digital audio.

CF: *You bring 25 years experience to Gibson. How will you use it?*
AC: By working in the trenches [Crudele was controller at Sports Authority before being appointed to CFO] you gain a thorough understanding of the critical nature of controls and how a breakdown can have a crippling effect. It also provides a more disciplined and organized approach to project management and day-to-day administration. This allows you to understand your business and grow it. As you gain experience, then you can lead. The glitz – IPO, M&A, debt deals – is great experience, but it's working with the operators that is the foundation stone of a strong CFO.

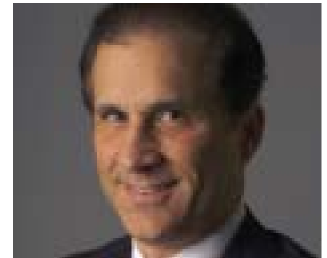
CF: *So how will you spend the early months at Gibson?*
AC: In my first year I will be focusing on harnessing the full power of our systems to provide financial information for real-time decision making. I also want to provide leadership to the finance area so that it is perceived as a value add partner. We are a decentralised organisation and I believe that we can highlight efficiencies throughout the organisation and enhance productivity.

Our sector has consistently had steady growth; but at Gibson we want to be a leader. We are constantly looking at advancements and have to be selective in how we allocate our resources. We have made a significant investment in two areas – developing the technology for a digital guitar and developing an extremely user friendly digital jukebox. Making sure we are properly capitalized and have the appropriate business partners to move these ventures forward was/is a priority.

CF: *What does 'properly capitalized' mean?*
AC: We have always leveraged our growth and have continued to do so. We recently completed a refinancing with two premier partners – Fleet Capital and Blackstone Partners. We look at our bankers as business partners. I consult with them on business issues and their varied backgrounds provide a strong experience base which is invaluable. Blackstone's equity and debt groups are premier Wall Street professionals and have access to resources that otherwise may not be accessible.

CF: *Do the scandals at public corporations affect the world of private corporations?*
AC: A lot has been said about accounting misappropriations and SEC scrutiny, but as a private company, we are focused on growing a business.

CF: *And do private investors differ from their public counterparts?*



"As you gain experience, then you can lead. The glitz of an IPO, M&A and debt deals is great, but it's working with the operators that is the foundation stone of a strong CFO."

AC: We have limited outside investors, but reacting to our board of directors and lenders is quite similar to dealing with outside investors. Questions will vary from general questions about the business to deep probing interrogations which require extensive analysis.

The most significant difference between us and a publicly traded company is the ability to share information more openly with our business partners and investors. In the public arena, you must ensure equitable dissemination of data to all parties; and therefore, you must be guarded in your comments prior to a general press release of the information.

CF: *So as the CFO of Gibson Guitars, can CF assume you play the instrument yourself?*
AC: I enjoy all types of music and would never want to do anything to harm the industry; therefore, I do not play any type of instrument! Growing up, my brother had a Gibson and a Gibson Amplifier. So my musical career ended on the best equipment. **RP**

Technophile CFO turns to TippingPoint

Adam Chibib, recently appointed CFO of TippingPoint Technologies, a provider of intrusion prevention technology - network security management to the IT illiterate - has made a successful career for himself in technology all without leaving Austin, Texas, his hometown since age 10.

Following a degree in business administration from the University of Texas at Austin, Chibib started his career in accountancy working for Franklin Federal Bancorp. But even then he had an inclination towards technology and was responsible for the company's successful conversion to new accounting software.

"Public accountancy was a great starting point for my career," says Chibib. "It taught me how to effectively solve different types of problems, at different companies, in different industries. From these collective experiences I was able to learn the best way to build operational infrastructure."

After stints at Coopers & Lybrand and Price Waterhouse where he was Technology Industry group manager, Chibib made the jump to software company Tivoli Systems. He was controller and responsible for the worldwide accounting functions of the multi-billion dollar company.

"What attracted me to technology companies was the chance to apply the techniques I had learned in public accountancy to the technology start-up environment. Technology companies provided me with the opportunity to build something from the ground up and have the responsibility for the success or failure of the companies that I work for."

That entrepreneurial spirit was given full rein when Chibib co-founded broadband software provider BroadJump in 1998. There he shaped the company by creating and implementing the business model, product licensing strategies and all internal policies and procedures. Under his guidance, the company maintained sequential quarter after quarter revenue growth, from its first revenue quarter in late 1999, and was profitable for the last three quarters of 2002 – two quarters ahead of schedule. BroadJump earned revenues of $50 million in 2002 – a 137% increase over 2001 – in very challenging economic times.

Those kind of results earned Chibib the 2002 Ernst & Young Entrepreneur of the Year Award and helped BroadJump achieve mention in Deloitte & Touche's "50 Fastest Growing Companies" list in 2001. They also made it possible for Chibib and his team to sell the company in November 2002 to Motive Communications, in a stock for stock transaction.

Not one to take the money and run, Chibib took over as CFO at WaveSet Technologies in May 2003. Seven months later WaveSet merged with Sun Microsystems and he moved on again. So why the move to TippingPoint which is, after all, a listed company and not a start-up? It comes down to his entrepreneurial personality, says Chibib.

"The entrepreneurial spirit is alive and well at TippingPoint," says Chibib. "The company is in a growth phase so the key fundamentals of my role have not really changed. I am still focused on shareholder value, accurate and timely internal and external financial reporting, compliance with applicable laws and smart growth. The opportunity at TippingPoint is as exciting and challenging as any start-up that I have worked for."

Chibib has spent most of his first four weeks at TippingPoint looking at the company's internal controls – "making sure that we are able to grow the company efficiently and effectively [by] having the right team in place, operational readiness, streamlined business processes and the right level of infrastructure."

Looking ahead, Chibib says that his financial goal for the company is to create shareholder value. He says: "Because we are an early stage revenue company, shareholder value will most likely be created through top-line revenue growth and driving the company to profitability. Our focus will be creating the right balance of investments to accomplish this."

"What attracted me to technology companies was the chance to apply the techniques I learned in public accountancy to a technology start-up."

But can TippingPoint ever achieve the amazing growth that BroadJump did? "The extraordinary growth at BroadJump was certainly atypical for the economic climate at that time. [However] I do see several similarities between BroadJump and TippingPoint that, coupled with an improving economy, may provide TippingPoint with growth opportunities.

"TippingPoint has done a tremendous job of defining the intrusion prevention market and creating a world-class product in UnityOne. [And] I think that our sector will see both validation and growth in 2004. Corporations will begin allocating budget dollars to intrusion prevention solutions and we will benefit from the maturation of our market," says Chibib. **MW**

ProxyMed recruits healthcare veteran

Starting a new job in the middle of a merger is probably every CFO's nightmare, but for Gregory Eisenhauer, newly appointed CFO of ProxyMed, the electronic healthcare transaction services company, its all real.

Denied the luxury of a honeymoon period, he has spent his first two months at ProxyMed dealing with an audit, and figuring out how to manage Sarbanes-Oxley.

"It's a lot to get up to speed on and the whole company is in a state of change. Anytime you move into a new field there is a whole new language to learn but I must say that everyone is very excited about the opportunities this merger will bring, and they have really helped my transition go quite smoothly."

The merger is with PlanVista Solutions, another healthcare claims service provider. The two companies signed a three-year joint marketing agreement in June 2003, a prelude to merging, but complemented each other so well they decided to complete the merger early.

Eisenhauer saw the benefits of the merger straight away. "It is cheaper and more efficient to process claims electronically rather than manually. But no one in the industry has put this together before, selling certain aspects of our services to providers and other aspects to payers. With PlanVista we will have a unique footprint.

"The merger allows us to expand the range of savings to medical cost management solutions."

The merger also puts both companies at the cutting edge when dealing with healthcare claims. "Healthcare lags behind other industries in using technology to make its processes more efficient. But the government will continue to apply pressure to the industry to increase the automation to reduce costs and errors."

Prior to ProxyMed, Eisenhauer worked for more traditional healthcare companies. He worked at RehabCare Group, a provider of therapy programme management and temporary healthcare staffing, ultimately becoming its CFO in September 2000. Eisenhauer was with RehabCare for almost 10 years and during his tenure there, revenues grew from $40 million to over $500 million. Eisenhauer left in May 2002 to became CFO for US Healthworks, a national occupational healthcare services company.

Eisenhauer is a healthcare veteran but like all the best career choices, it wasn't planned. His first job was with APEX Oil and Sverdrup Corporation, a provider of technology engineering services. He moved to RehabCare when his boss at Sverdrup became RehabCare's CFO.

Similarly, Eisenhauer knew ProxyMed CEO Mike Hoover and Nancy Ham, president and COO, before moving there. He is content to stay. "Healthcare is a growing field. [At ProxyMed] I liked the space, the growth opportunities and the management. It was the right time to join. I am fortunate to be joining a company that represents such an exceptional growth opportunity." **MW**

In brief

»The New York Stock Exchange board of directors has appointed **Amy Butte** as executive vice president with plans for her to succeed **Keith Helsby** as CFO when he retires in April. Most recently Butte was chief strategist and CFO of Credit Suisse First Boston's financial-services division.

»Uniform provider Angelica Corporation's CFO **Theodore Armstrong** has retired after 18 years with the company. **James Shaffer**, who has been with Angelica for nearly five years as vice president and treasurer, will succeed Armstrong as CFO.

»Generic drug maker Andrx has promoted former finance VP **John Hanson** to CFO. Former CFO **Angelo Malahias** has become president.

»United Technologies, a provider of products and services to the building systems and aerospace industries, has appointed two vice presidents to assume the responsibilities of CFO **Stephen Page** when he retires on April 14. **James Geisler** has been named vice president, finance and **Gregory Hayes** has been named VP, accounting and control.

»Discount retailer TJX Companies has named **Jeffrey Naylor**, former CFO of Big Lots, CFO. Former CFO **Donald Campbell** assumes the newly created position of executive vice president, chief administrative and business development officer.

»**Mary Winston**, most recently vice president and controller of Visteon Corporation, has been named as CFO of Scholastic Corporation. **Kevin McEnery**, who held this position since 1995, resigned to pursue new career opportunities.

»Apple executive vice president and CFO **Fred Anderson** will retire on June 1 2004 and hand the reins over to senior vice president of finance and corporate controller **Peter Oppenheimer**. Anderson will be appointed to the board of directors upon his retirement. He currently serves on the board of eBay and E.piphany.

CFO PROFILE

"Financing €68 billion debt was the easy bit."

In December 2002 France Telecom had €68 billion in debt and was being bailed out by the French Government. A year later debt has reduced by a third and the company is successfully playing the capital markets. **Tabitha Neville** talks to Michel Combes, the modest finance chief at the centre of it all.

ILLUSTRATION: RUSS TUDOR

"2003 was a good year in terms of revenue growth. It was a year in which France Telecom took control of its destiny again."

It is fair to say that France Telecom has had a difficult couple of years. In fact, it is probably an understatement when you look closely at how far the company had fallen down the financial black hole and how far it has had to travel to get out of it. There isn't a better turnaround story around.

The teleocm company spent about €80 billion ($97.5 billion) in cash on expansion between 1999 and 2000 (it has 11.7 million customers over five continents) and racked up more than €100 billion debt. Plans to refinance and reduce the company's debt were not implemented due to the market turnaround and by April 2001 the company's share price had fallen 70% and debt had ballooned to €60 billion (preceding the fall, France Telecom's (FT) shares had climbed 200% in less than six months).

In December 2002, the French government advanced a €9 billion loan to help the company out of its deepening financial crisis, and to prevent it missing a €15 billion debt repayment in 2003. For 2002, FT reported a record full year loss of €20.7 billion.

In February 2004, the company reported revenues of €46.1 billion. The company's full-year net profit was €3.2 billion a €23.9 billion turnaround from 2002. Group debt amounted to €45 billion at the end of 2003 compared to €68 billion a year earlier.

CF caught up with Michel Combes, CFO of France Telecom, on the day the company issued a €2.5 billion three tranche deal in euros and sterling. After a year's absence the company's bonds were oversubscribed across all three maturities – the £500 million tranche was three times oversubscribed and the €750 million eight-year tranche four times – which enabled the company's bookrunners DrKW, HSBC, JPMorgan, SG and Natexis to increase all three tranches. The banks were delighted with the deal's reception but Combes plays its success down.

"Markets are generally good at the beginning of the year, and the reception our issuance received is a reflection of this and of the scarcity of corporate bonds coming to market."

FT 2005: break down

France Telecom launched FT 2005, in December 2002. It was an initiative comprising four components:

» TOP: a program to improve operational performance, which will generate more than €15 billion in free cash flow to reduce debt for the period 2003-2005;

» "15+15+15": a plan to strengthen the group's financial structure;

» €15 billion via the TOP program;

» €15 billion in fresh equity, with the participation of the French State in its capacity as shareholder pro rata to its shareholding interest, i.e. for approximately €9 billion;

» €15 billion euros from refinancing debt;

» A strategy focused on customer satisfaction and integrated operational management of a portfolio of assets comprising businesses that are leaders in their principal markets, with strong brands such as France Telecom, Orange, Wanadoo and Equant. Assets with weak strategic and financial positions or those for which majority control is not possible will be considered for divestment. France Telecom will pursue strategic partnerships in areas outside its core activities or those where it cannot achieve critical mass;

» A completely new management team led by Thierry Breton,with a simplified organization and greater responsibility assigned to managers.

Just over a year later, the company has reduced its on-balance-sheet net debt by €23.8 billion to €44.2 billion. The TOP indicator "Operating income before depreciation and amortization less Capex" increased by 66.1% on a comparable basis (63.4% on a historical basis), to reach €12.2 billion at December 31, 2003.

The €2.5 billion issue was a technical refinancing move, and a liability management exercise, says Combes; a debt optimisation process. "The conditions of the three tranches are better than the average cost of debt for FT at the tme and it was not a question of liquidity but a question of reprofiling debt and rebalancing currencies. We had low reimbursement in 2007 and 2008 and no reimbursement in 2012, 2013 and 2014. The bond improves this maturity profile. It was an opportunistic move by us [FT is cash flow generative and positive and has no need for funds] and allowed us to strike a better balance between our euro and sterling debt. Our sterling cash generation is rising and it seemed an appropriate time for increase in sterling denominated debt."

More importantly, the success of the bond demonstrated the quality of FT's credit and the financial markets' vote of confidence in FT's financial health. It was also further vindication of the company's management, turnaround plans and execution. It is a long way from the state of affairs in December 2002, when FT struggled to raise financing in the capital markets and avoid a liquidity crisis. "We were facing such huge reimbursement amounts that the markets were effectively closed to us.

"What has been achieved in the last 12 months is due to a dedicated management team with clear strategic goals and strong execution skills," says Combes.

On December 4 2002, the same day the French government agreed its €9 billion bailout of the company, Thierry Breton, CEO, announced the initiative that was to turn the company around.

Called the FT2005, the initiative included: TOP – a program to improve operational performance and generate more than €15 billion in free cash flow to reduce debt; and 15+15+15 – a plan to strengthen the group's financial structure through the TOP program, raising €15 billion in equity and €15 billion from refinancing the company's debt (see box). The majority of savings in 2003 concerned optimization of investments and working capital

"The rating in itself is not a commitment of the management team. Our objective is a net debt/EBITDA ratio of between 1.5 and two by the end of 2005."

requirements. Additional free cash flow would be generated from fixed-line activities in France (40% to 45%) and by Orange (35% to 45%). Wanadoo will account for less than three per cent of the total.

The company also aimed to achieve greater strategic and financial flexibility with the aim of a net debt/EBITDA ratio of between 1.5 and two by the end of 2005.

It was an ambitious plan, admits Combes, but the market believed in it and, as a consequence, reopened to the company in December 2002.

France Telecom wasted no time in acting upon the new initiative and addressing its liquidity crisis. On 11 December 2002, it issued a €2.5 billion, seven year eurobond. This was followed up in January 2003 with a €5.5 billion bond which covered the refinancing of debt maturing in 2003. In February, the company secured the signing of a new three-year syndicated credit facility for €5 billion. It was a turning point for the company.

"The liquidity crisis that was facing us at the end of 2002 was over by February 2003." In late February, FT's shareholders approved plans for equity issuance of up to €30 billion and on March 24, the company launched its long-awaited €15bn ($15.9bn) rights issue, representing the third tranche of its €45bn rescue plan. Some €9bn of the issue was taken up by Erap, a public body that holds the industrial stakes of the French state, which owns 54.5% of France Telecom.

In its Q1 2003 results, released in April 2003, FT achieved an EBITDA margin of 36.2% (32% 2002) and EBITDA net of capital expenditure reached 27% of sales compared to 15% in 2002. Almost immediately, S&P raised its long and short-term corporate credit rating on FT to BBB from BBB- and A-2 to A-3 (S&P has just raised its long-term outlook to BBB+). Fitch swiftly followed. For a company that saw its credit rating go from the top to the bottom of the investment grade scale between 1996 and 2002, this was a tremendous achievement.

"The rating in itself is not a commitment of the management team," says Combe, who reemphasizes that the. company's objective and commitment vis a vis the financial markets is to reach a net debt/EBITDA ratio of between 1.5 and two by the end of 2005. "This level of leverage will mean we have the same leverage as a single A rated company. The rating therefore is only a result of our commitment. The spreads we got on our bond issue this January reflects the good assessment of FT credit quality by the market.

"It signals that the company is operating as a normal company again and that the market believes in FT and believes in our future in telecoms. I am proud to be working for one of the main European players again." cf

Orange & Wanadoo buy-outs

France Telecom is one of the few telecom operators with a presence in wireless (Orange), the internet (Wanadoo), fixed-line services and corporate solutions. It has managed this through an aggressive acquisition policy which surfaced late in 2003, when it bought out Orange shareholders and in February when it put forward a proposal to do the same for Wanadoo shareholders.

In September 2003, FT agreed to pay €7.1 billion in stock to buy-out minority shareholders in Orange – just 30 months after it spun its mobile subsidiary off.

This move reflected the rapid return to health of FT and the move to reverse the decentralised make-up of the company which, CEO Thierry Breton claims, did not let the group take maximum advantage of the potential synergies across different business lines.

"Orange is core to FT's strategy and that is why we decided to buyout Orange minority shareholders and take over full ownership of the company," says Combes.

In February, FT launched a $4.9 billion offer of cash and stock for the remaining 29.4% of Wanadoo – it currently owns 71% of the company.

Wanadoo has seen its shares rise over 60% in the last year and reported net income of €159 million in 2003, up from €30 million in 2002 and it has long been expected that FT would make moves to squeeze out the minority shareholders.

The deal, to be followed by a listing of Wanadoo's Yellow Pages directory business, will enable the French State to reduce its stake in FT to 50% from 54.5%. (A law was passed in December 2003 allowing the French Government to decrease its stake in France Telecom. It has yet to declare its intention to do so).

The offer put forward by the company values Wanadoo at €13.25 billion ($16.56 billion).

COMBES'S CAREER PATH

» Michel Combes, 40, began his career at France Telecom in **1986** working on external networks and industrial and international affairs. In **January 2003**, he was appointed CFO.

» In **February 2004**, Combes stepped down as non-executive director of Eurotunnel citing an increased workload at France Telecom.

» In **1991** he was appointed technical advisor to the Minister of Post, Telecommunications and Space, then to the Minister of Public Works, Transport and Tourism. He returned to France Telecom in **June 1995**.

» Combes was executive vice president of the Nouvelles Frontières Group from **December 1999** to the end of **2001**.

Getting to grips with technology puzzles

As a corporate treasurer how do you manage to stay abreast of developments in the world of payments and messaging standardization? With so many different organisations entering the market **Robert Pink** decided to take stock.

Hands up those who know what TWIST, SWIFT, FIX, Identrus, Eleanor and RosettaNet are about. There aren't many of you, are there? Well, let *CF* explain. They are all organisations pushing for standardized messaging in the corporate and banking spheres.

Of the six groups, only TWIST and RosettaNet are directly open to corporate membership, but all of them can influence the daily working life of you the corporate treasurer.

Applying new message standards around the commercial payments process based on XML can bring the following additional benefits to corporates:

» increased process transparency through tracking of payments based on status information provided by the banks;

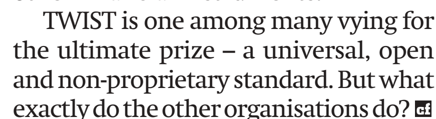
» improved STP in reconciling accounts receivable to payments received through automatically delivered remittance details that are uniquely linked to payment transactions;

» improved opportunities for cash positioning and working capital financing, based on the effective use of information available on future payments.

"Corporate treasurers spend 90% of their time involved in the internal provision of liquidity and gathering liquidity, so for a treasurer his neck is on the line for 90% of the time," says Tom Buschman, development manager at Shell Finance Services. If this is the case, then the liquidity improvements the organisations promise by way of improving business processes for the global trade lifecycle, will be an important weapon for the treasurer.

Buschman is one of the driving forces behind TWIST, a relative newcomer in the world of payments organisations. TWIST – or the treasury workstation integration standards team – was founded in 2001 and boasts 70 members including treasury industry bodies and investment banks. Its avowed goal is to create a not-for-profit industry group driving towards open and universal standards to allow corporate treasurers to communicate with their banks, brokers and electronic trading platforms for FX and other financial instruments.

TWIST is one among many vying for the ultimate prize – a universal, open and non-proprietary standard. But what exactly do the other organisations do?



SWIFT – Society for Worldwide Interbank Financial Telecommunication.
What is it?: Its prime objective is to contribute to the commercial success of its members through greater automation of the end-to-end financial transaction process. It aims to be the global financial community's foremost messaging infrastructure of lowest risk and highest resilience.

FIX – Financial Information Exchange Protocol.
What is it ?: A message standard for real-time electronic exchange of securities transactions.

Identrus
What is it?: An identity management, policy and standard definition setting organisation establishing rules and processes for technology, risk management, legal contracts and business practice in the course of business-to-business e-commerce. It aims to assist organisations, including corporates, to apply identity authentication.

Eleanor
What is it?: An Identrus initiative to introduce secure, direct business-to-business payments on the internet.

RosettaNet
What is it?: An electronic messaging standard and an industry group setting messaging standards and business processes for its members; its core members exist primarily in the Asian market.

It aims to create and implement industry wide, open ebusiness process standards.

The value creation equation

The mantra of shareholder value gained sway years ago. But which companies have embraced the concepts behind managing for shareholder value? And how do you measure it anyway? Working with global consultant Stern Stewart, *CF* has endeavoured to find out. **Tabitha Neville** reports.

Business journalists, from their first day on the job, are told to leave their prejudices at the door of the office. Just because a reporter's car isn't working doesn't mean he can lay into Ford next time its results are released.

Nevertheless it was with a certain degree of *schadenfreude* that I spoke to Chaith Kondragunta, co-managing director of Stern Stewart Europe, two weeks before we published this issue.

He calls me to talk about *CF* and Stern Stewart's survey of the top 25 companies in Europe, the US, and Japan. At the same time, I'm on hold on my mobile phone to Vodafone, the world's largest mobile telecom company. Having switched over to their network a week before, I'm already on my third call to customer service.

"You should have asked them about their poor MVA performance," jokes Kondragunta.

"I don't think customer service worry about such things," I reply.

"No, but their management will."

The *schadenfreude* resulted from the revelation that Vodafone is ranked 25 in *CF's* survey of the top 25 corporates in Europe by market value added (MVA) performance.

To be fair, coming bottom of a top 25 poll is still something of an achievement – they beat many other companies, of course. But Vodafone's lack of attentiveness in customer service seemed – to me at least – to be a reasonable metaphor for a negative MVA figure of 142,865 – well below Vivendi Universal's negative MVA of 37,963, which is ranked at 24. Kondragunta doesn't seem surprised by Vodafone's ranking. "The only surprise would have been if Vodafone hadn't been at the bottom of the list."

As global consultants, Stern Stewart helps companies develop a systematic

What is…

»MVA

Mathematically MVA is the difference between market value – calculated as the sum of the market value of equity, debt and the market value of outstanding stock options – and the company's invested capital – the cash investors, both equity- and debt-holders, contributed to the company's operations. A high MVA indicates the company has created substantial wealth for shareholders. MVA is equivalent to the present value of all future expected EVAs. A positive MVA indicates that investors expect the company to generate significant amounts of EVA in the future. A company with a negative EVA but positive MVA can mean one of several things: the market expects it to turnaround; that it may be a potential takeover candidate; or that it is following a business cycle.

»EVA

Economic value added (EVA) is an estimate of true "economic" profit, or the amount by which earnings exceed or fall short of the required minimum rate of return that shareholders and lenders could get by investing in securities of comparable risk. In its simplest form it's a company's trading profit – net operating profit after taxes paid (NOPAT) minus a capital charge for both debt and equity. Stern Stewart has made changes in the caluculation of profit and capital to make the result more realistic. It capitalises investments in intangible assets placing them on the balance sheet where they belong.

Top 25 Japan (by market value)

	Company Name	Industry	MVA	Market Value	Capital	EVA	NOPAT	ROCE
1	NTT DoCoMo Inc	Communications	56,603	95,349	38,746	915	3,310	8.54%
2	Takeda Chemical Inds	Pharmaceuticals	20,097	30,871	10,774	1,512	1,834	19.52%
3	Toyota Motor	Transport Equipment	19,277	132,370	113,092	2,784	6,683	6.74%
4	Canon	Electrical Machinery	15,386	30,337	14,950	658	1,515	10.24%
5	East Japan Railway	Land Transport	7,993	30,335	22,343	1,074	1,690	7.46%
6	Tokyo Electric Power	Electric Power and Gas	7,662	84,747	77,085	246	2,149	2.65%
7	Nissan Motor	Transport Equipment	6,742	49,083	42,341	2,082	3,306	7.84%
8	Sony	Electrical Machinery	6,570	37,262	30,692	(1,446)	813	2.54%
9	Honda Motor	Transport Equipment	5,385	47,738	42,353	1,856	3,076	8.14%
10	KDDI	Communication	3,736	22,612	18,877	(468)	670	3.41%
11	Chubu Electric Power	Electric Power and Gas	2,972	40,111	37,139	431	1,315	3.46%
12	Kansai Electric Power	Electric Power and Gas	2,570	40,886	38,316	365	1,294	3.30%
13	Kyushu Electric Power	Electric Power and Gas	626	23,434	22,808	197	747	3.12%
14	Tohoku Electric Power	Electric Power and Gas	600	22,510	21,910	319	852	3.71%
15	Toshiba	Electrical Machinery	155	21,722	21,567	(507)	455	2.05%
16	Itochu	Wholesale	(817)	25,317	26,134	(194)	616	2.27%
17	Mitsui	Wholesale	(935)	35,421	36,356	(176)	675	1.87%
18	Mitsubishi	Wholesale	(1,013)	41,283	42,297	(134)	861	2.04%
19	Nippon Steel	Steel Products	(1,155)	22,259	23,414	(245)	441	1.84%
20	Nippon Telg. and Tel.	Communication	(1,580)	113,082	114,662	(277)	4,796	4.14%
21	Marubeni	Wholesale	(2,481)	23,778	26,259	(128)	492	1.68%
22	Sumitomo	Wholesale	(2,844)	28,639	31,483	(350)	479	1.71%
23	Fujitsu	Electrical Machinery	(6,209)	20,101	26,311	(1,309)	190	0.73%
24	Hitachi	Electrical Machinery	(10,567)	37,477	48,043	(1,778)	593	1.21%
25	Matsushita Electrical	Electrical Machinery	(12,622)	26,789	39,411	(953)	642	1.62%

Market value as of 31 March 2003
Capital as of 31 March 2003, year-end operating capital
Exchange rate as of 31 March 2003, EUR per JPY 0.00776, source Bloomberg
Excludes banks, insurance and other financial institutions

SOURCE: STERN STEWART

focus on creating shareholder value through its MVA/EVA (see box) performance ratios. The firm was the perfect choice to help *CF* create a ranking of top performing companies.

Both MVA and EVA are value-based metrics, which have grown in popularity as traditional accounting metrics have been proven to be unreliable. MVA is the difference between the market value of a company (both equity and debt) and the capital entrusted to it. Put simply it is the difference between 'cash in' (what investors have contributed) and 'cash out' (what they could get by selling at today's prices). The true aim of a company should be to maximise MVA rather than the value of the company – as this can be easily achieved by investing increasing amounts of capital.

EVA essentially reflects the difference between a company's achieved net operating profit (NOPAT) in any given year and the net operating profit it needed to achieve in that year in order to compensate shareholders for the cost of capital.

Show me the money

Finance executives have been spouting platitudes about shareholder value for as long as most business consultants can remember. As a consequence of this familiarity, there is a sizeable contingent of detractors – not least because many companies only appear to pay lip service to it.

The faith that the market had in shareholder value, and the methods of achieving it, has taken a severe beating over the past five years. Corporate governance scandals, endless downgrades and executives massaging figures dominated the headlines and undermined confidence further.

But the happy consequence of these rather distasteful events has been

CFOS LEADING JAPAN

NTT DoCoMo Keiji Tachikawa
Takeda Chemical Hiroshi Takahara
Toyota Motor Fujio Cho
Canon Toshizo Tanaka
East Japan Railway Masatake Matsuda
Tokyo Electric Power Shigemi Tamura
Nissan Motor Carlos Ghosn
Sony Nobuyuki Idei
Honda Motor Takeo Fukui
KDDI Tadashi Onodera
Chubu Electric Power Takatoshi Fujitani
Kansai Electric Power Hiroshi Morimoto
Kyushu Electric Power Michisada Kamata
Tohoku Electric Power Yasumasa Makuta
Toshiba Tadashi Okamura
Itochu Sumitaka Fujita
Mitsui Tasuku Kondo
Mitsubishi Ichiro Mizuno
Nippon Steel Akira Chihaya
Nippon Telg. and Tel. Toyohiko Takabe
Marubeni Nobuo Katsumata
Sumitomo Motoyuki Oka
Fujitsu Hiroaki Kurokawa
Hitachi Takashi Miyoshi
Matsushita Electrical Kunio Nakamura

Top 25 Europe (by market value)

	Company Name	Industry	MVA	Market Value	Capital	EVA	NOPAT	ROCE
1	Shell combined	Oil Comp - Integrated	93,946	195,314	90,772	6,125	12,416	15.9%
2	GSK	Medical - Drugs	86,968	121,994	37,503	6,347	9,107	25.7%
3	BP PLC	Oil Comp - Integrated	69,006	192,160	112,251	144	8,786	8.0%
4	Novartis	Medical - Drugs	59,662	96,985	37,260	2,743	5,252	13.8%
5	Nokia OYJ	Telecoms Equipment	56,686	73,530	16,671	2,429	3,852	24.6%
6	Nestle SA	Food-Misc	52,254	103,950	51,136	3,953	7,082	13.6%
7	Total SA	Oil Comp - Integrated	51,952	114,630	65,399	1,798	6,703	11.3%
8	Roche Holding	Medical - Drugs	43,661	89,207	42,126	(1,203)	1,742	4.0%
9	ENI SPA	Oil Comp - Integrated	28,990	84,195	53,111	1,471	5,729	11.0%
10	Unilever Group	Food-Misc	27,541	62,008	33,839	1,494	4,292	11.5%
11	Carrefour SA	Food-Retail	21,978	44,808	21,947	621	2,435	10.5%
12	Orange SA	Cellular Telecom	16,757	39,844	22,676	(6,049)	(3,819)	-15.4%
13	Siemens AG	Diversified	11,999	52,082	39,542	(1,031)	2,244	5.4%
14	Philips Electronics	Electonic Compo	11,548	31,170	19,443	(4,925)	(2,907)	-13.2%
15	France Telecom	Telephone - Integrated	11,360	113,852	92,711	(29,954)	(18,476)	-18.0%
16	ENEL SPA	Electric - Integrated	9,877	63,308	53,360	(1,289)	2,694	5.2%
17	BASF AG	Chemicals	8,556	32,077	23,125	249	2,043	8.9%
18	Tesco PLC	Food-Retail	8,143	26,609	18,404	305	1,776	10.1%
19	E. ON AG	Electric - Integrated	5,132	99,743	88,101	(5,408)	789	1.0%
20	Telefonica SA	Telephone - Integrated	4,834	83,745	73,398	(6,053)	996	1.3%
21	DaimlerChrysler AG	Autocars/Light Trucks	248	139,642	138,962	(9,128)	5,521	3.8%
22	Deutsche Telekom AG	Telephone - Integrated	(2,005)	125,748	123,764	(20,258)	(7,559)	-5.6%
23	Telecom Italia S	Telephone - Integrated	(17,723)	65,550	74,288	(4,638)	3,557	4.5%
24	Vivendi Universal SA	Media	(37,963)	50,621	83,087	(10,413)	(1,938)	-1.9%
25	Vodafone Group	Cellular Telecom	(143,865)	150,541	295,675	(11,676)	11,130	4.1%

Market value as of 31 December 2002
Capital as of 31 December 2002, year-end operating capital
Exchange rate as of 31 December 2002, EUR per USD 0.9531, source Bloomberg
Excludes banks, insurance and other financial institutions

SOURCE: STERN STEWART

greater assertiveness by shareholders. They are more eager than ever to discover exactly how much value corporate management has added to their investment capital and spelling out what it is that the management team should be credited with achieving.

Value Based Management, based on MVA/EVA, is a management approach that ensures corporations are run consistently on value – and normally on maximising shareholder value. It includes creating value, managing for value and measuring value. It uses simple transparent metrics that not only highlight where a company has added or destroyed shareholder value but gives investors a good indication of how capable the management team is.

Define shareholder value?

Nurturing the conditions to best create shareholder wealth is harder than you might think. Boards can often lack a shared perspective on how stock markets evaluates corporate performance. Equally, they may not fully understand the key strategic factors for creating value in today's market. That's where the CFO is meant to step in.

The CFO has traditionally served as a company's shareholder value steward. He is often the first to introduce core value principles, is the one pushing for the resources, methodologies and – most importantly – management time required to make 'value´ work. It is inevitably he who argues that effective company-wide programmes will return many times the initial investment. So if a CFO is the shareholder value steward, then a positive MVA/EVA is surely a credit to his strong leadership, clarity of focus and firm controls over cash.

But what is shareholder value? "Shareholder value is why we come to work everyday," says Pat Mulva, head of IR at Exxon Mobil, the world's largest oil company (which does not have a CFO, by the way). "Everyday we compete for that investment dollar and it is our job to provide value to the people making that investment decision everyday."

Mulva defines shareholder value as the appreciation of the share price and the long-term impact of dividends and share buy-backs. In 2002, Exxon distributed more than $10 billion to

CFOS LEADING EUROPE

Shell Judith Boynton
GSK John Coombe
BP Byron Grote
Novartis Raymond Breu
Nokia Olli Pekka Kallasvuo
Nestle Wolfgang H Reichenberger
Total Robert Castaigne
Roche Holding Erich Hunziker
ENI Marco Mangiagalli
Unilever Rudy Markham
Carrefour Jose-Luis Duran
Orange Wilfried Verstraete
Siemens Heinz-Joachim Neuburger
Philips Jan H M Hommen
France Telecom Michel Combes
ENEL Fulvio Conti
BASF Kurt Bock
Tesco Andrew Higginson (FD)
E.ON Erhard Schipporeit
Telefonica Santiago Valbuena
DaimlerChrysler Dr Manfred Gentz
Deutsche Telekom Karl-Gerhard Eick
Telecom Italia Enrico Parazzini
Vivendi Sandrine Dufour
Vodafone Kenneth Hydon

Top 25 US (by market value)

	Company Name	Industry	MVA	Market Value	Capital	EVA	NOPAT	ROCE
1	Microsoft Corp	Software & Services	208,888	233,329	24,441	1,025	4,371	17.75%
2	General Electric Co	Capital Goods	174,786	269,547	94,760	5,667	12,930	14.51%
3	Wal-Mart Stores	Retailing	174,198	244,370	70,171	2,797	8,652	13.03%
4	Johnson & Johnson	Pharmaceuticals	110,938	156,298	45,360	2,706	6,785	15.01%
5	Merck & Co	Pharmaceuticals	98,803	134,590	35,787	3,690	6,771	19.12%
6	Coca-Cola Co	Food	87,701	110,671	22,971	2,331	3,847	17.46%
7	Procter & Gamble Co	Household	85,514	125,333	39,818	1,835	4,824	12.99%
8	Exxon Mobil Corp	Energy	80,422	260,108	179,686	(2,072)	11,685	6.61%
9	Intl Business Machines	Technology Hardware	71,650	170,328	98,678	(7,655)	3,517	3.66%
10	Dell Computer Corp	Technology Hardware	60,659	67,533	6,874	356	1,229	17.64%
11	Intel Corp	Technology Hardware	56,961	92,397	35,436	(3,560)	2,282	6.25%
12	United Parcel Service Inc	Transportation	54,968	74,327	19,359	834	2,457	13.05%
13	Lilly (Eli) & Co	Pharmaceuticals	54,390	70,969	16,579	1,045	2,396	15.52%
14	Pfizer Inc	Pharmaceuticals	50,114	183,869	133,755	(3,367)	8,759	6.59%
15	Pepsico Inc	Food	47,326	77,093	29,767	1,032	3,073	10.55%
16	Altria Group Inc	Food	47,158	117,027	69,868	5,705	9,951	14.25%
17	Cisco Systems Inc	Technology Hardware	45,156	89,180	44,025	(5,616)	566	1.30%
18	Bellsouth Corp	Telecomms	21,488	67,993	46,505	(1,225)	3,697	7.76%
19	Verizon Communications	Telecomms	18,446	193,812	175,366	(5,349)	12,285	7.04%
20	Chevrontexaco Corp	Energy	6,725	92,812	86,087	(2,991)	3,248	3.76%
21	Viacom Inc -Cl B	Media	5,960	90,482	84,522	(4,854)	2,924	3.46%
22	General Motors Corp	Automobiles	(14,724)	99,437	114,161	(6,014)	2,058	1.80%
23	SBC Communications Inc	Telecomms	(24,649)	124,922	149,571	(8,287)	7,190	4.82%
24	AT&T Corp	Telecomms	(61,066)	78,583	139,649	(27,148)	(12,982)	-8.70%
25	AOL Time Warner Inc	Media	(79,113)	95,276	174,389	(31,211)	(14,360)	-8.01%

NOTE:
Market value as of 31 December 2002
Capital as of 31 December 2002, year-end operating capital
Exchange rate as of 31 December 2002, EUR per USD 0.9531, source Bloomberg
Excludes banks, insurance and other financial institutions

SOURCE: STERN STEWART

shareholders through dividends and share buybacks. In 2002, its dividend increased for the 20th consecutive year.

There is little disagreement with this basic definition. Ladislas Paszkiewicz, head of IR at oil company Total, agrees with Mulva's definition of shareholder value as the sum of a contribution of stock performance and yield through dividend. Likewise, a spokesman at Novartis, the Swiss-based pharmaceutical giant asserts that, "The ultimate measure [of shareholder value] is the development of the share price, dividend pay outs and value of spin offs."

But Paszkiewicz also says that shareholder value is simply a by-product of how well (or badly) a company performs. "At Total, shareholder value is the result of our emphasis to improve company performance. We control what we deliver through the company's internal plans that focus on growth and productivity. This translates into shareholder value creation. The two are linked."

Exxon's overriding objective is to create sustainable shareholder value by seeking high returns at low risk and focussing on the long-term, says Mulva. "Exxon has an investment discipline, operational excellence and is careful where it invests. Exxon's standards of investment discipline have consistently delivered superior returns demonstrating we are using [investor's] capital wisely and creating long-term sustainable growth and value."

Novartis takes a similar approach. "Novartis is committed to shareholder value but on a sustainable basis, not just for optimising short term measures," It attributes its success to a clear focus on sustainable growth, a corresponding, consistently innovation-oriented strategy, and the capabilities and commitment of its management.

Interestingly, pharmaceutical companies, which feature strongly in the listing, perform well in MVA measures because of their investment in R&D. "MVA is made up of the future cash line of the company," says Stern Stewart

CFOS LEADING US

Microsoft John Connors
General Electric Dennis Dammerman
Wal-Mart Stores Thomas Schoewe
Johnson & Johnson Robert Darretta
Merck Judy Lewent
Coca-Cola Gary Fayard
Procter & Gamble Clayton Daley
Exxon Mobil N/A
Intl Business Machines John Joyce
Dell Computer James Schneider
Intel Andy Bryant
United Parcel Service Scott Davis
(Eli)Lilly Charles Golden
Pfizer David Shedlarz
Pepsico Indra Noovi
Altria Group Dinyar Devitre
Cisco Systems Dennis Powell
Bellsouth Ronald Dykes
Verizon Comms Doreen Toben
Chevrontexaco John Watson
Viacom Richard Bressler
General Motors John Devine
SBC Comms Randall Stephenson
AT&T Thomas Horton
AOL Time Warner Wayne Pace

Philips

Royal Philips Electronics, the third largest global consumer electronics maker, has been using EVA as an instrument to measure financial performance since 1997.

Philips recognized that the normal net income profit and loss account didn't account for a company's cost of capital, says group controller Gerard Ruizendaal. "We wanted to make it visible so we could understand this cost." EVA has since been ingrained in the company's standards and is based on the cost of capital that in each activity, reflects the risk related to the business, geography and effective tax rates. "The main idea is to improve our EVA every year so our return of capital is more than our cost of capital," says Ruizendaal.

One of Ruizendaal's main responsibilities as group controller is performance management, "looking at systems, metrics, and how to measure the value of our strategies."

Philips measures value creation on a strategic level and for investments through net present value techniques, says Ruizendaal. At the operating level, value creation is measured via EVA. "With EVA you don't look to short-term movements in share prices, but to consistently improving the returns above the cost of capital."

EVA is not the exclusive measurement tool at Philips. The company also uses the business balance scorecard. Ruizendaal explains: "Current financial performance is essentially a consequence of what you have achieved in the past in the business, so we try to correlate this financial performance with leading non-financial drivers such as customer satisfaction based measurements and process based measurements." (eg, on supply chain performance).

"All the decision making tools must be consistent for driving value creation within the company, and with every year, with every process, it becomes a way of life.

Philips also looks at how to integrate EVA into its staff incentive structure, with EVA accounting for approximately 50% of the criteria for yearly bonus incentives. "The amount of share options offered to employees depends on the share performance versus 24 benchmarked companies, and the incentives are less if we don't outperform against our benchmark peers."

Over the last two years, Philips has systematically changed its portfolios to businesses with return of capital greater than the cost of capital. Gerard Kleisterlee, president, emphasized this in his message in the company's 2003 annual report, saying, that over the past year Philips had made considerable progress on its journey to create One Philips - a single, focused and clearly identifiable company geared to sustained value creation.

Europe's Kondragunta. "There is a lot more future growth associated with companies with high R&D so naturally they have a higher MVA."

Value creation

An analysis of investments in the shares of Stern Stewart's publicly-owned US clients showed they produced 49% more wealth after five years than equal investments in shares of competitors with similar market capitalisations. How?

As a company you are committed to shareholder value creation. But do you understand where and how value is being created and where opportunities for value creation lie? MVA, EVA and value-based management companies do, says Kondragunta, and that is why those US companies produce 49% wealth.

Managers, and this essentially means the CFO, at value-based management companies believe that there are only three basic ways to increase and manage value. The first is to increase the returns from the assets already in the business by running the income statement more efficiently without investing new capital. The second is to invest additional capital and aggressively build the business so long as expected returns on new investments exceed the cost of capital. And the third is to release capital from existing operations, both by selling assets that are worth more to others and by increasing the efficiency of capital by such measures as turning working capital faster and speeding up cycle times.

Total and Exxon do not subscribe to value-based management, but both firmly believe that the culture, strategy and financial controls of value-based management are firmly in place at their companies.

"We have a global functional organisation operationally consistent throughout. It is this consistent approach that embraces the core principles at Exxon," says Mulva.

Exxon subscribes to a high return and low risk strategy, "not overcapitalising on investment [but] being focused on the long-term," says Mulva. It is an approach that has steered the company throughout its history, and enabled it to outperform its competitors over the past 20 years. So how does Exxon measure the value its core principles bring? Through return on capital employed (ROCE - income before financial items relative to average capital employed). "Shareholders entrust us with their capital and we tell them how well we have managed it through ROCE. People understand ROCE. It is a very powerful," says Mulva.

It is a similar tale at Total. "We run the company from an industrial viewpoint. We allocate cash in an efficient manner and measure through return on average capital employed." (ROACE - operating profit before amortization of goodwill x 100/ average invested capital, accumulated amortization of goodwill). "It is a consistent measure of shareholder value in our industry and allows our investors to compare like with like." In its 2003 report, Total

offered a cash dividend of €4.7 a share – a 15% increase on 2002. The ROACE was 19% in 2003 – the highest level among its competitors.

Reward Processes

Shareholders invest in people. They entrust people with their capital. But shareholders have learnt to their cost that they can be too trusting.

At the heart of the recent spate of corporate scandals are employees manipulating figures for their own gain. As financial incentives to achieve targets have become more attractive more employees have massaged the figures to achieve them.

Until recently, granting stock options had potentially hazardous implications for long-term success at a company. Firstly, in a rising market they tend to reward management that isn't necessarily creating shareholder value and may even be destroying it. Secondly, they focus attention on the short-term – the perception that value has been created becomes as important as creating value. Hence, the incentive to massage figures.

How pay is tied to performance is a thorny issue, but the structure of financial incentives has a key part to play in preventing such corporate misdemeanours from happening again. "Using EVA and MVA allows less room for gaming," says Kondragunta.

Because EVA can be measured at any point in an organisation, bonuses linked to EVA are a powerful influence on corporate behaviour as you are aligning an employee's interests to the long-term value creation expected by investors. "The no improvements, no pay-off approach will incentivise employees to seek out truly profitable growth opportunities rather than investing in wealth destroying ventures," says Kondragunta. Acquiring companies at high premiums while never realising adequate returns on the capital employed is a good example. EVA will capture the fact that profit is growing but not fast enough to compensate the rise in capital invested.

"We are all paid on the basis of performance with a long-term view," says Mulva. "It is a broad-based incentive scheme based on how we perform as a company and how we perform onan individual basis." Novartis sees no antagonism between a company's share price performance and internal incentive and bonus schemes. "A rising stock price will in the long run reflect the value creation. There is no contradiction between the two."

The true value of a good conversation

Value-based management has been credited with many things: increased transparency, lower capital costs, more accurate forecasting and improved decision making. But Exxon Mobil's Mulva says that the real key to improving shareholder value is communicating with shareholders, investors, and the market. In fact just about everyone.

"It is essential to communicate to our shareholders," he says. "You can't just have one annual meeting and one annual report." Exxon has increased its face-to-face public meetings and says it has increased its output of information ten-fold, as its website testifies. If communication is the key, then the CFOs at corporates we contacted are doing a sterling job. The CFOs at Total, Nokia, Roche and Novartis were on trips gladhanding shareholders when *CF* called

Siemens

Siemens introduced EVA in 1997. "It requires managers to radically rethink all business decisions and to forget ROI and measure profitability with an eye on the cost of capital," said Dr Karl Hermann Baumann, CFO back in 1997. He credits the introduction of EVA with helping to turn Siemens around.

Siemens has a positive economic value added (EVA) of €449 million in fiscal 2003, an improvement of €768 million compared to the prior year's figure of a negative €319 million, excluding a €936 million tax-free gain on the sale of shares in Infineon. Including this gain, EVA for fiscal 2002 was a positive €617 million.

"Shareholder value is about a strong performance oriented culture and creating a sustainable economic value – not only on a day-to-day-level – but on a sustainable basis in the long term," says Sabine Kromer, corporate communications officer at Siemens. "A central aim for Siemens, as it was defined by our CEO Mr. v. Pierer in the companywide Ten-Point Program in the year 2000, is to generate a positive economic value added (EVA) and to improve it further.

"We see innovation as a main driver for shareholder value in our daily business," says Kromer. "At the beginning of fiscal 2004 we decided to concentrate on three company-wide programs: innovation, customers focus and global competitiveness. As part of our innovation program, we will focus more on developing trendsetting technologies and cross-group technology platforms. With our customer focus program we intend to substantially boost growth, but not at the expense of earnings. Global competitiveness to us means that we plan to expand our presence at lower cost locations. This means purchasing, manufacturing, software development and administrative services."

ABOUT STERN STEWART

Stern Stewart is a global consulting firm that specializes in helping client companies in the measurement and creation of shareholder wealth through the application of tools based on modern financial theory. The company pioneered the development of its proprietary EVA® (Economic Value Added) framework, which offers a consistent approach to setting goals and measuring performance, communicating with investors, evaluating strategies, allocating capital, valuing acquisitions, and determining incentive bonuses that make managers think like owners.

cf

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How accurate are FX forecasts?

Every month financial institutions across the UK provide *CF* with their FX and interest-rate predictions. But how accurate are they? **Jason Eden** analyses the submissions for 2003 and reveals who is *CF*'s FX Forecaster of the Year.

The past 12 months haven't been easy for FX forecasters. The war in Iraq, SARS and only a fledgling recovery of the world's economies have kept many of them on their toes.

But, judging by the results of the analysis of FX forecasts published in *CF* during 2003, some of the forecasters out there have done a damn good job, despite these difficulties. (Some, to be fair, have done a pretty poor job, but we'll leave you to work out who has egg over their face).

So, the results are in and for the first time in four years, *CF* is pleased to announce a new titleholder of its FX Forecaster of the year trophy. Or, to be more precise, two new titleholders. Royal Bank of Scotland's (RBoS) forecasting duo Neil Parker, marketing strategist for G7 countries, and Adrian Schmidt, senior currency strategist, have toppled Societe Generale's Bob Eveling from the top spot he has held for the past three years.

"We are very pleased to be number one. We believe it is due, in part, to the close working relationship that Adrian and me have at RBoS," says Parker. And RBoS deserves its place at the top of the league table. Not only was it the overall winner, but it placed first in cable and €-JPY – two currency pairs that saw some serious volatility during 2003 - and finished in the top five of all the currency pairs we categorised in our league tables. "RBoS would expect to do very well in cable, as it is our home market. We feel confident in predicting what drives this currency pair," says Schmidt.

METHODOLOGY

The methodology consists as follows: Each month the participants forecast where the spot rate will be in 3 months time. We have taken the mid-month spot rate for each applicable month and awarded the 10 nearest forecasters points starting from 10 for a first place, down to one for 10th place. *CF* chose to rank forecasters by total points, not average points, hence rewarding those who have been most diligent in providing forecasts each month.

A volatile market - maybe

Depending on which forecaster you talk to, 2003 was either a very volatile year or pretty flat. Such varying views may explain the array of forecasts *CF* receives every month.

"Volumes were massive in 2003," says Trevor Williams, chief economist, financial market division at Lloyds TSB, "largely due to the volatility." And Williams predicts 2004 to be as interesting, and busy, a year. "The globalisation of the world economy means an increase in trade, and with China and Russia joining in, capital markets expanding and volatility rising." Parker agrees: "The volatility is self-evident by the see-sawing we've seen in the currency markets and the scale and speed of the moves during 2003. Moving forward, we'd expect volatility to be high this year as well, although perhaps slightly lower than last year. Moves will remain abrupt and large by recent historical standards."

Bob Eveling, senior vice president, FX and derivative sales at Societe Generale, disagrees with both Parker and Williams: "Volatility levels became relatively flat as it became obvious the USD was a one-way bet, i.e. it would go down. Apart from brief flurries on profit-taking driven orders in general, volatility was quiet."

OVERALL BEST FX FORECASTER BANK

	Total Points	Frequency	Average points
RBoS	236	36	5.88
Lloyds	228	37	6.16
Societe Generale	222	42	5.42
SEB	203	28	7.25
Commerzbank	201	37	5.43
UBS	184	33	6.90
Citigroup	181	28	6.46
AMEX	168	23	7.30
CSFB	137	24	5.71

USD weakening

For most analysts, developing a weakening dollar strategy was the key to a successful 2003. Parker, for example,

Do you manage FX exposure?

Currency volatility is an issue that concerns the finance department in every large corporation across the globe, and the recent instances of a depreciating dollar and a strengthening euro over the last year provide ample evidence of the kind of challenges they face.

But how can a corporate treasurer gain greater understanding of currency fluctuation or access independent price discovery and analytical tools for the FX options markets? *CF* decided to sit down with GFI Group, an inter-dealer brokerage, market data and analytical software provider for the global cash markets, to get the inside view.

Activity in the currency options business is rising, largely due to the levels of volatility that GFI has seen in the FX markets over the last 12 months. This volatility in FX increases the need for hedging and therefore the demand for pricing tools, such as GFI's FENICS® FX.

So why is FENICS® FX such a good option for corporate treasurers?

GFI's FENICS® FX has over 15 years experience delivering transparent and independent front-office pricing and analysis software to the majority of banks active in FX options. But increasingly corporate treasurers of varying market caps are looking to adopt this kind of technology to manage their company's currency risk exposure. Nicola Williamson, the FENICS® FX product manager explains: "While some corporates engage in currency hedging transactions of millions of dollars a day, any company hedging their currency exposure with FX options would have use for FENICS® FX."

FENICS® FX has a range of analytical tools allowing users to perform "what if" analysis. It also runs the critical reports required for instant overview of currency derivative profiles and the system can be customised and integrated with corporates' middle and back offices.

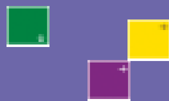
Judging from its existing client base the prospects for the product seem strong. As Fiat notes: "We value FENICS® FX because it offers us an independent and accurate tool for pricing and revaluing vanilla and exotic currency options"

"FENICS® FX also delivers independent data," asserts Michel Everaert, global head of product development and marketing. "As a broker which does not take market positions, GFI is ideally positioned to provide corporate treasurers with hard-to-find, independent, real time and historical market data." Demand for GFI's data services, particularly its popular daily Revaluations Fixing initiative, is expected to grow over the coming months in response to new accounting standards requiring market participants to mark their derivatives positions to market. Corporate treasurers might have the technology and advice from their banking partners but they also need the independent and objective perspective as well.

Pricing derivatives needs an independent model and independent data inputs. Everaert adds: "FASB 133 affects how you account for your derivatives. As a treasurer you have to specify if you are using a hedging or speculative trade. If you can't account for the trade as a hedge you have to use a mark-to-market rate – in other words the rate has to be 'market observable'. That's where GFI steps in. Treasurers need a market observable price for their trades."

The installation of FENICS® FX can also compliment the relationship between a corporate and its bank. Because the product is widely used in the industry it means major banks are conversant with the technology. "You'd be hard pushed to find professionals in the industry who aren't well-versed in the use of FENICS® FX", points out Williamson.

FENICS® FX



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Banana skins for 2004

It is early days, but what are the events corporates should be keeping an eye on when deciding their FX strategy over the coming months?

On the political front, Trevor Williams at Lloyds TSB is keeping tabs on the presidential elections in the US. "The obvious political banana-skin is the US presidential election in November. It is difficult to call who will win at this juncture." Bob Eveling at Societe Generale, on the other hand, doesn't see much fall-out from the elections. "If Kerry is elected then the status quo will be maintained in the USA," he says.

Neil Parker at RBoS is concerned with affairs nearer home. "The UK government has come in for plenty of political pressure of late [two-fifths of the labour government would like to see Tony Blair, PM, quit before the next election according to recent reports in the press] and its standing in the polls has suffered accordingly. We may see a surprise election."

On the economic front, Parker and Eveling are in agreement. "As far as

"If Kerry is elected then the status quo will be maintained in the USA."

economic banana-skins are concerned, the risks surrounding the Chinese economy and currency and the potential for revaluation of the yuan (or a move in the peg) could create turmoil in currency markets," says Parker. For Williams it is the "continuing upside risk to the euro," that is causing him most concern. "A strengthening euro will not help the euro zone export their way forward throughout 2004," he says.

attributes his success to "predicting the weakening dollar trend very early on".

The dollar fell steadily against most of its major trading partners throughout the latter half of 2003, including the euro and the Japanese yen.

"The momentum of the dollar depreciation at year-end 2003 caught me by surprise," says Michael Schubert, senior economist at Commerzbank, "because this development was out of line with the behaviour of the fundamental factors." Eveling, who was ranked first in 2000, 2001 and 2002, but who is placed third this year, admits it caught him on the hop too. "I have to be honest here and say that rather than develop a weakening USD strategy, it was thrust upon me. My basis for predicting the future rate does rather depend on spot levels at the time, so consequently as the USD weakened my predictions would as a matter of course lead to a weakening USD scenario."

The factor most cited as the cause for an on-going fall of the US currency is the unsustainability of the huge US current account, says Williams, who forecast dollar weakness early in 2003.

"The current account deficit is causing a major problem for the US economy and its currency level," says Williams. "I wonder how the US government is going to keep the current account deficit under control and stop it getting to a level where drastic measures have to be taken." The downside isn't over yet, he adds, saying dollar weakness has another 10% to go.

Schubert disagrees with Williams that the US current account is the cause of the dollars fall. "Our analysis shows that at least until November, the development of the dollar versus the euro could be well explained by other factors. Estimating the dollar-euro exchange rate on the basis of relative sector productivity differences and the 10-year bond yield spreads leads to an average estimation error of just two per cent. It would be premature to conclude that the exchange rate during 2003 was mainly driven by the market's perception of the unsustainability of the current account deficit.

"The dollar's decline has developed a momentum of its own, which we feel has transformed into speculative exag-

€-USD

	Total	Position	Frequency	Average
Lloyds	41	1	6	6.83
RBS	41	1	6	6.83
Citigroup	36	3	5	7.20
AMEX	35	4	4	8.75
Commerzbank	32	5	6	5.33
CSFB	29	6	5	5.80
UBS	28	7	5	5.60
Bank Montreal	27	8	4	6.75
SocGen	27	8	6	4.50
HSBC	26	10	3	8.67

USD-JPY

	Total	Position	Frequency	Average
SocGen	48	1	8	6.00
Lloyds	45	2	7	6.43
SEB	43	3	6	7.17
UBS	36	4	6	6.00
RBoS	29	5	4	7.25
Deutsche Bank	27	6	4	6.75
HSBC	26	7	4	6.50
AMEX	25	8	4	6.25
CSFB	25	8	4	6.25
JPMorgan	24	10	4	6.00

£-USD

	Total	Position	Frequency	Average
RBoS	41	1	7	5.86
SEB	40	2	5	8.00
Lloyds	35	3	6	5.83
SocGen	35	3	6	5.83
Citigroup	30	5	5	6.00
Commerzbank	27	6	7	3.86
AMEX	23	7	4	5.75
CSFB	23	7	4	5.75
HSBC	23	7	4	5.75
Deutsche Bank	22	10	3	7.33

€-JPY

	Total	Position	Frequency	Average
RBoS	52	1	7	7.43
SocGen	39	2	7	5.57
AMEX	32	3	4	8.00
Lloyds	32	3	6	5.33
SEB	31	5	5	6.20
UBS	29	6	6	4.83
ABN	28	7	4	7.00
Citigroup	28	7	5	5.60
Commerzbank	28	7	6	4.67
CSFB	26	10	4	6.50

€-CHF

	Total	Position	Frequency	Average
Commerzbank	54	1	7	7.71
Lloyds	45	2	7	6.43
SEB	39	3	6	6.50
RBoS	38	4	6	6.33
SocGen	37	5	6	6.17
Citigroup	31	6	4	7.75
JPMorgan	30	7	4	7.50
AMEX	28	8	4	7.00
UBS	24	9	5	4.80
Deutsche	21	10	3	7.00

What a corporate needs

The modern corporate treasurer operates within a risk-averse environment. The treasury is run not as a profit-centre operation, but as a cost-centre department. It is accountable for its bottom-line.

"Very few corporate clients run FX profit-centres, as they do not appear to have the time to run positions and cover their needs for the company," says Bob Eveling of Societe Generale.

So, how have the changes of focus and operations within treasury affected its FX requirements?

"We have seen a divergence away from the standard vanilla products into a more structured approach to hedging FX positions," says Neil Parker at Royal Bank of Scotland. Mans Grunberger of SEB agrees: "We cannot identify any major changes in hedging techniques during the last couple of years, but corporate clients have become more sophisticated in combining instruments.

Eveling claims FX options have become part of their corporate clients' arsenal against FX exposure but in *CF's* FX Survey in its October issue, some of the criticisms levelled at the banks were that the banks were offering structures and products that were too sophisticated and that they were over-promising and under-delivering. "We send out the best strategy best suited for our clients. On a weekly / monthly basis we continue to provide our in-house forecasts and economic views. We also provide our own ideas on FX rates and moves on a daily basis via direct contact on the telephone."

Trevor Williams at Lloyds TSB would not accept such criticisms. "We aim to provide a service corporates want; a service which involves charts, keeping a close eye on volatility and early-warning signs of trend movements as well as any upside or downside risk that we feel a client needs to be aware of."

Demand varies, says Grunberger. "Some corporates want a short-term view which relies mainly on technical analysis, flow analysis and market behaviour, whilst the majority of our corporate clients have a medium or long-term view and would like analysis which combines market behaviour and positioning, structural capital flows, macro fundamentals, political analysis."

Whatever the corporate need, be it short- or long term, says Michael Schubert, at Commerzbank, the key for any successful client-bank relationship is consistency. "Consistency in our forecasts is important. We try to elaborate in our reports the various interdependencies between the variables mentioned. It is necessary that the amount of depreciation or appreciation we predict for a currency is quantifiable from the client's point of view and that changes in our forecasts are comprehensive."

geration, but which will be the more difficult to halt the longer it lasts. Our assessment does mean that there is a serious risk of the dollar losing further ground as long as there are - besides the concern that the US current-account deficit is no longer sustainable - other reasons (yield spreads, doubts about the durability of the US recovery) suggesting that the dollar is unlikely to make up for its losses."

Yen going from strength to strength

A good FX forecast can act as an early-warning signal to off-set future liabilities. The USD-JPY currency pair is a good example. Forecasting the resurgence in strength of the Japanese yen would have been very profitable to many of the banks' corporate clients in the past 12 months, who generate profits in yen but later repatriate into dollars. Equally, a good relationship with your FX forecaster may have convinced you to take out a forward contract to pay for goods that you intended to purchase later on in the year. "If the Bank of Japan hadn't intervened," says Williams, "I could see USD-JPY trading as low as 100 or even 95. It certainly would have damaged their recovery."

USD-CHF

	Total	Position	Frequency	Average
Commerzbank	40	1	6	6.67
RBoS	37	2	6	6.17
Citigroup	35	3	5	7.00
Lloyds	34	4	6	5.67
SocGen	32	5	7	4.57
SEB	31	6	5	6.20
UBS	29	7	5	5.80
AMEX	26	8	3	8.67
JPMorgan	26	8	4	6.50
Goldmans	24	10	3	8.00

Williams admits to being taken by surprise by the Bank of Japan's action. "I was very much surprised by how far the Bank of Japan intervened. They needed to prevent further deflationary bias against the yen, but I was still surprised by the amount of dollars they bought." So what other currencies caught our forecasters off-guard?

Parker and Schmidt say the South African rand and the Turkish lira, while Eveling looks to the euro. "I expected a recovery when it broke back through parity in early December 2002. I expected it to stabilise at around 1.18, which I consider fair value for the currency." The current high level of the euro will, he adds, be detrimental to a recovery in the euro zone.

Mans Grunberger of SEB on the other hand was shocked by the impressive strength of the Australian dollar. "Despite some question marks about the global economic recovery, geopolitics and Australia's poor external balances, the AUD has been supported by strong productivity growth."

CF would like to congratulate the top 10 forecasters of 2003. It was a difficult year, with some unexpected currency movements. *CF* would also like to thank the industrious forecasters who continue to reply to our monthly requests for information. It is extremely appreciated. cf

How are you funding your WCM needs?

The CP market is the ideal short-term debt financing solution. It is cheap for the issuer and low risk for the investor. But a fall in ratings and economic stagnation has knocked the wind out of CP and investor appetite. And, if CP is no longer an option what are the alternatives? **Robert Pink** reports.

Is the commercial break over for US commercial paper?" That was the question raised by S&P in March 2002. The US commercial paper market had undergone its largest contraction in 40 years and the outstanding market stood at $1.35 trillion – the lowest level since the last quarter of 1999 and 6.1% down on the year-end for 2001.

"As business investment picks up steam," asserted a bullish S&P, "working capital requirements will accelerate among firms, in turn fuelling increased demand for commercial paper."

Market players, hoping for good news, heaved a sigh of relief and looked forward to a return to normality.

Almost two years later the US market has further contracted to around $1.3 trillion, although the European market has continued growing. So what are the corporates using to finance their short-term debt needs? Commercial paper, say banks.

Why CP remains top

Commercial paper is used by large corporates, with high credit ratings (and low investment risk), to finance day-to-day working capital management needs such as accounts receivable and inventory. It is available in a wide range of denominations, can be either discounted or interest-bearing, and usually has a limited or nonexistent secondary market. Maturities typically range from two to 270 days. It is sold to money market funds, banks, institutional investors and corporates.

"Corporates have become increasingly large investors in short-term paper," says Arnaud Achour, head of corporate debt origination at SG CIB. "They have built up enormous stock piles of cash as a consequence of their deleveraging efforts."

"The advantage [of CP] over bank financing – where interest rates may float two to three per cent above the base rate – is that the cost of borrowing [with CP] is at Libor flat or less," says Colin Withers, managing director of short-term products at Citibank. It is also flexible – allowing a company to match financing needs directly with cash flow. Libor stands for the London Interbank Offered Rate and is the rate of interest at which banks borrow funds from other banks, in marketable size, in the London interbank market.

"Commercial paper offers a high grade of flexibility and a very deep market," says Norbert Mayer, head of corporate financing at the BMW Group. As head of corporate finance, Mayer is responsible for corporate strategy on short-term debt financing. BMW uses a mixture of CP and the short-end of the MTN programme for its short-term needs, says Mayer. "Having direct contact with the investors is part of BMW's funding strategy. Bank loans are not that important for us."

For Mayer, commercial paper is still a viable option, but the figures released by S&P suggest BMW is one of the few remaining corporates to be able to access the market.

Corporate ECP Issuance from 1 Jan 2002 to 1 March 2004

Rank	Issuer	USD Eqv (at issue) m	Trade	%Share
1	Unilever NV	81,100.34	1,134	8.33
2	E.ON AG	52,057.91	761	5.35
3	Eni Coordination Center SA	37,926.09	480	3.90
4	Coordination Center Volkswagen SA	32,643.47	1,604	3.35
5	KarstadtQuelle AG	26,058.33	1,521	2.68
6	Deutsche Telekom AG	23,472.18	851	2.41
7	DaimlerChrysler AG	20,514.38	997	2.11
8	RWE AG	17,368.86	387	1.78
9	Tesco plc	16,738.54	327	1.72
10	METRO AG	16,711.12	792	1.72
	Total	**973,440.10**	**31,145**	**100.00**

Source: Dealogic

Norbert Mayer, BMW: "Commercial paper offers a high-grade of flexibility and a very deep market. Having direct contact with the investor is part of BMW's funding strategy. Bank loans are not important to us."

The ratings game

"The decrease [in the market] has been due to three factors," says Steve Huntley, head of money markets at Bank of America. "Firstly, issuers 'terming out' commercial paper balances in the long-term debt market; secondly, decreasing needs for working capital management; and thirdly ratings downgrades."

Commercial paper is only issued by large corporates with high credit ratings – BMW has short-term debt ratings of A-1 from S&P and P-1 from Moodys – the best short-term rating it offers.

Large multinationals with an A1-P1 rating, such as BMW, often use both the European and US commercial paper market. That gives them access to a potential investor base of $6 to 7 billion in short-term debt in this year's market.

"The only risk for corporates raising money in the short-term debt markets is if the market closes," says Achour. "In the past there have been some corporates who have relied too heavily on the short-term finance markets. They have then been faced with liquidity problems when downgraded because the market had closed on them."

Withers agrees: "An A2-P2 issuer can still get $2-3 billion in the US markets but once a company starts a ratings slide the availability of funds dries up [investors will start backing out] and it slides into bank financing at more expensive borrowing rates."

In 2002 Tyco lost a reported $400 million after losing the confidence of institutional investors in its commercial paper programme.

Amid investor concerns about accounting at the firm, the conglomerate had to draw on a backup line of credit from its banks to come up with the cash it needed. The move to replace cheap commercial paper with the more expensive bank line cost Tyco about $400 million in additional after-tax annual borrowing expenses, slicing about five cents per share from first-quarter earnings, which were expected to come in at 80 cents per share. According to Withers, the ratings slide began long before Tyco's accounting troubles. In January 2001. "There were a few surprises from Californian utilities followed by downgrades in the telecoms and automotive sectors." Prominent US issuers of commercial paper programmes downgraded in 2003 would be too numerous to mention, but they include Cargill, Eastman Chemical, Carnival and Schering-Plough.

"In the corporate bond market if you lose one notch rating you will still have access to the investors, but in the commercial paper market you could end up being completely cut off, especially on non-domestic programmes," says Achour.

"The majority of short-durations are pooled vehicles, generally rated AAA, and we have to invest a large percentage of our cash in higher rated not lower rated vehicles," says Wayne Bowers, the director of global fixed income at Northern Trust Global Investors (NTGI). "If you look at the cost-client mandate we manage, one of the requirements is the 'preservation of principle'. If you have money held in the short-term the last thing you want is to suffer a fall in your investment. The level of risk on duration and the risk perspective is very limited."

Not all domestic markets are as strict as the US market. "The European market is more forgiving," says JC Perrig, Bank of America's head

THE CF GUIDE TO SHORT-TERM DEBT

»Operating term loans: used for working capital management to cover inventories, monthly expenses, interest on outstanding loans, rent, utilities, leases.
»Revolving lines of credit: a credit facility which allows the borrower, within a credit limit and for a set period, to borrow or repay debt as required.
»Revolving loan: a loan where the borrower decides the number and timing of withdrawals against the bank loan; any money repaid may be re-used at a future date. (A line of credit where the customer pays a commitment fee and is then allowed to take and repay funds at will. It is usually used for operating purposes, fluctuating each month depending on revenues and expenditures.)
»Commercial paper: used by corporates to issue short-term IOUs for short-term financing – lasting up to 270 days or just one day only. Commercial paper invariably doesn't require any guarantees and is the cheapest source of debt financing. Rates are typically below longer-term bonds and loans from banks, largely because it is less risky to lend money for such a (relatively) short time period in which it is so much easier to predict the fortunes of the company.

Bank ECP Issuance from 1 Jan 2002 to 1 March 2004

Rank	Programme Dealers	USD Eqv (at issue) m	Trade	%Share
1	Deutsche Bank	10,153.29	1,507	13.41
2	Citigroup	9,192.56	1,330	12.15
3	Barclays Capital	7,583.72	1,274	10.02
4	UBS	7,262.38	1,141	9.60
5	JP Morgan	5,188.88	918	6.86
6	Goldman Sachs & Co	5,185.36	820	6.85
7	Royal Bank of Scotland	5,020.43	759	6.63
8	ING	3,410.30	800	4.51
9	Credit Suisse First Boston	2,381.00	516	3.15
10	Lehman Brothers	2,343.23	465	3.10
	Total	**75,686.62**	**2,102**	**100.00**

Source: Dealogic

of international debt capital markets, "especially in Germany and France. Name recognition still stands for a lot more in Europe where as in the US the market is driven by hard ratings.

"The credit markets in Europe have matured a lot and can make the distinction between an isolated event and the broader environment. A one-off credit incident doesn't fundamentally change the picture."

Securitization: the alternative option

The increasing number of downgrades over the last two years, combined with a global slowdown and falling interest rates, may have been bad news for straight commercial paper but alternative methods of short-term financing, such as securitization, have benefited. By borrowing money against defined revenue streams, issuers can access funding at costs which would otherwise be unavailable to them.

In December 2003, the US securitization market was worth €625 billion, in Europe €98 billion. In Europe, the asset-backed commercial paper sector is about 25% of the total commercial paper market and in the US it represents over $700 billion or 55% of the total commercial paper market.

Rick Pelini, Lexmark: "Lexmark doesn't have a traditional commercial paper programme. We choose to fund our short-term needs through a securitized receivables programme."

"The good thing about securitization is that for corporates rated BBB or below it's cheap money for them," says Achour. "Using securitization isn't too cost effective for A-rated corporates, but it's a good complementary short term funding [strategy]."

Huntley agrees. "Corporates with lower ratings will use asset-backed securitization as a source of off-sheet balance sheet funding that is attractively priced."

One corporate treasurer to take advantage of securitizaton is US oil company Weatherford. The company does not run a commercial paper programme because, "the company would probably be an A2-P2 issuer, meaning less access to investor cash," says treasurer Joe Gocke.

Instead it has an asset-backed accounts receivable programme. "We began the programme in 2001, primarily as a less expensive source of funding," says Gocke. The programme operates in the US, a source of a third of Weatherford's revenues. "Weatherford does business in 100 countries around the world so the administrational costs of an asset-backed programme in all of these countries would be prohibitive," he explains.

Rick Pelini controls treasury operations at Lexmark, the US printing solution provider. He tells a similar story. "Lexmark doesn't have a traditional commercial paper programme. Instead, we choose to fund our short-term working capital needs through a securitized receivables programme. This provides access to the stable A1/P1 commercial paper market at prices only slightly higher than actually having an A1/P1 programme.

"Because of our excess cash position, Lexmark doesn't actively manage a short-term versus long-term debt portfolio. Our overall philosophy is to ensure adequate lines of credit through bank revolvers (we currently have $500

Janet Hargreaves, treasurer at Balfour Beatty and MMF

Balfour Beatty provides civil engineering and design services to rail, road and utility systems. It's short-term needs are great.

"Our short-term borrowings are all on the money markets or on an overdraft – we don't use commercial paper as we don't have a public rating and don't really think it's worthwhile to do so," says Janet Hargreaves who heads up the treasury team.

"We monitor cash on a daily basis and know within a month when we're going to be short of cash," she says. "The flexibility of the money markets is the main advantage – I can raise money for any period from overnight to one week to six months."

According to Sander Boelen, global head of liquidity management at ABN AMRO, the money markets are maturing fast and there is a growing appetite for the funds.

"There has been a shift from corporates to corporates to corporates to money market funds. Falling interest rates have helped encourage this, as have recent high profile corporate fraud cases."

More and more corporate treasurers are asking themselves: "Do I want to invest this money myself or outsource the capital to diversify. The first concern for the treasurer is capital preservation. Personally, I don't believe that a treasurer should be going after every last basis point."

"His [the treasurer's] second concern is liquidity. "Can I get my capital back when I need it? Return on capital is not the main driver in most cases. It is liquidity and the streamlining of the treasury. The funds allow you to be part of a larger group of investors which gives economies of scale. The other thing you buy is the whole risk management system behind it. When there is two per cent interest for a piece of paper there is not much room to play with if things go wrong."

Weatherford chooses loan flexibility

"The capital markets are very wide open right now, both from a banking perspective and a capital markets perspective," says Joe Gocke, treasurer at US-based oil company Weatherford, "It's a function of the general economy in the US more than anything else. As companies look to produce more and make more acquisitions it naturally leads to a need to access the capital markets."

Weatherford doesn't use the CP markets, says Gocke – they have a $500 million revolving credit facility and an asset-backed accounts receivable programme. "We don't use them, firstly because we would be an A2-P2 issuer and this market is not as deep as the A1-P1+ market and secondly, because we would only be infrequent users of the market." Instead, Gocke uses bank loans to fund the company's short-term debt needs. "The bank market is a little more expensive than commercial paper programmes but we then would have to go to the trouble of setting it up and then rarely using it. A banking facility allows us immediate access to funds; it is not dependent on ratings." Weatherford is also paying down short-term debt at the moment and deleveraging, says Gocke, so it wouldn't make sense to start a commercial paper programme.

million of unused revolver capacity) and the receivables securitization. Five years ago the company issued $150 million of ten-year notes which remain outstanding."

Looking ahead

So where is the market heading? S&P continues to predict an upturn in the US corporate commercial paper market. "The steady erosion in US non-financial commercial paper outstanding appears to be at a plateau with economic indicators hinting that corporations will have an increased need to tap external sources – namely commercial paper and bank loans – to finance working capital," says Diana Vazza, managing director of global fixed income research at S&P.

Achour agrees: "Some corporates are reactivating their short-term debt instrument programmes. They want to be ready in case their working capital needs increase. If the economic recovery speeds up then working capital needs will also increase. In the past few years corporates have restructured back to their core businesses – they are now slim and cash rich."

But, the low interest rate environment makes bank lending more attractive than ever. "Bank debt usually provides a convenient source of funding with as much capacity as a corporate needs to finance its requirement," says Perrig. "The present environment for bank-debt is very attractive for borrowers as the spreads are so narrow. In the long-term however, structural changes in the bank market means that bank funding will become scarce."

JC Perrig, Bank of America: "The present environment for bank-debt is very attractive for borrowers as the spreads are so narrow. In the long-term however, structural changes in the bank market means that bank funding will become scarce."

He is of course referring to Basel II. Basel II aims to maintain the overall level of capital in the global banking system while aligning it more closely with the underlying risks of a bank's activities, i.e. by basing minimum capital requirement on the credit ratings of borrowers. In a nut shell what this means is that banks will not lend funds to a corporate unless it can be sure of sufficient profitability on the accounts at the same time it is providing credit facilities.

"Banks are changing their approach to lending. They focus on the most efficient use of their equity, hence, for the future, bank borrowing will be a less attractive source of funding compared to commercial paper. The commercial paper situation will stabilize and the short-term market will develop towards the commercial paper market once again," says Mayer.

Rick Pelini at Lexmark agrees: "There is a trend among corporates to reduce reliance on banks and to pursue other sources of capital. This is logical given the mergers that have taken place in the banking community; net bank lending capacity has declined and will probably continue to do so."

"Corporates are finding that lines from the banks are drying up and the cost of borrowing is increasing. In response they are creating their own CP programmes," adds Brian Farrell, global head of money markets at DEPFA bank. cf

Corporate ECP Outstanding as at 1 March 2004

Rank	Programme Dealers	USD Eqv (at issue) m	Trade	%Share
1	Unilever NV	4,489.80	96	5.93
2	Eni Coordination Center SA	3,578.70	47	4.73
3	Volkswagen AG	3,436.20	45	4.54
4	Network Rail CP Finance plc	3,180.02	71	4.20
5	E.ON AG	2,532.11	60	3.35
6	RWE AG	2,000.80	30	2.64
7	Enel Investment Holding BV	1,834.66	59	2.42
8	Procter & Gamble Co	1,766.46	24	2.33
9	Pfizer Inc	1,764.33	15	2.33
10	Housing Finance Agency Plc	1,715.60	28	2.27
	Total	**75,686.62**	**2,102**	**100.00**

Source: Dealogic

Manchester SSCene

Manchester has long been an industrial and financial hub in the north of England. But, says **Robert Pink**, it is a SSC location too.

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In 1783, Richard Arkwright, inventor of the Spinning Jenny and father of the industrial revolution, built his first textile factory in Manchester.

Based in the north of England, the city quickly became a hub for the textile industry, and a premier industrial centre.

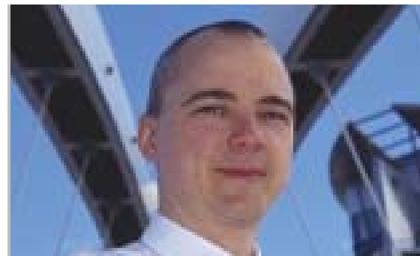
Two hundred years later and the textile factories have disappeared. In their place? Sophisticated shared service centres.

Multinationals have traditionally looked to sites in London, Amsterdam or Dublin to locate their European shared service centres, but recognising the investment such centres bring to an area, other European cities threw their hats in to the ring. Manchester was one such city.

Manchester's rise

In 1997, MIDAS – the Manchester Investment and Development Agency Service – was created to promote the city as a viable alternative to London or Dublin.

"We identified Manchester as a shared services location because Manchester shared the same labour force characteristics as places like Dublin and Glasgow," says Chris Norwood, development manager at MIDAS. Location consultants perceived that Dublin and Glasgow were over-heating and were looking around for the next big thing in SSC location selection, he adds, and MIDAS put forward an offer based around the availability of customer service languages and technical skills as well as a large international airport. It must have been persuasive. Georgia Pacific set up its SSC in Manchester in 1998, Tetrapak in 1999, and AstraZeneca in 2001.



Chris Norwood, business development manager at MIDAS: "We identified Manchester as a shared services location because it shared the same labour characteristics as places like Dublin and Glasgow."

Popular shared service locations can become victims of their own success. Too many corporates join the party, the employee base shrinks and costs rise. That happened in Dublin, says Norwood, and MIDAS is working hard not to allow it to happen in Manchester.

"In 1998 eight SSCs arrived in Dublin at the same time and attrition in some companies rose to 75%. The 'fear' of going to a location that would overheat became a major feature of location selection. Location consultants have been trying to write Manchester off as 'overheated' for the last five years every time we have won a project.

"The Manchester SSC community has grown incrementally over that time and the 'exceptional' attrition levels and associated salary inflation that reached in Dublin five years ago have not been witnessed here (or in many other successful locations)."

To mitigate the prospect of Manchester's 'over-heating', MIDAS has created a shared services forum to discuss best practice on a quarterly basis. Norwood hopes this will foster a shared service community and will stop any staff poaching; there are agreements in place on salary benchmarking to help the process along.

Employing capital

Manchester is located in one of Europe's most heavily populated regions, which means corporates located there are able to call on a large employment pool. The city supports 90,000 students at any one

JT International

JT International announced the opening of its Manchester-based European Business Service Centre in February 2003. As a subsidiary of Japan Tobacco – the world's third largest cigarette manufacturer – JT International boasts sales in excess of $30 billion.

JT International (JTI) is a shared service professional. As the t-shirt says, "Been there, done that". In addition to Manchester, the company has one in Kuala Lumpur, managing the Asian market, and one in St. Petersburg, for dealing with the Russian market where the company has a particularly strong presence.

The choice for a European location was between sites such as Manchester, Barcelona, Rotterdam, Dublin and Prague. For Martin Braddock, JTI's CFO, the creation of a shared service centre in Europe was linked to an overall corporate strategy: "Throughout the process, JTI was trying to become a low-cost quality producer. That applied to the product itself as well as the back-office functions. This drove the thinking towards a shared service centre."

The employee base was top priority. "The criteria for the shared service centre was essentially the availability of labour, the skill of labour and the cost of labour. We formerly evaluated the Netherlands and our St. Petersburg operations but we discounted a number of other locations as we were moving very quickly.

"We heard Dublin was over-heating in terms of its shared services and that we'd be moving in to a zoo, competing for staff. In Barcelona we heard there were problems with retaining the right quantity and quality of staff and in Prague there were similar concerns." So why Manchester?

A grant from the North West Development Agency (NWDA) of £630,000 ($1.2 million) proved a good incentive, as did cooperation offered by the Manchester Investment and Development Agency Services (MIDAS). "The grant was not the over-riding factor in our decision, but it did indicate an acceptance by the NWDA of our moving in to the area. In some countries the development agencies were only luke-warm in their reception."

The challenge for Braddock was the conceptual change. "Any shared service centre experience is difficult - you're

"Throughout the process JTI was trying to become a low-cost quality producer. That applied to the product itself as well as the back-office functions."

changing processes, systems and organisation. We did the process in 12 months but it was very painful."

After his experiences in creating a shared service centre, what advice does he have for a CFO setting out on the shared service route? "You can't do enough planning, you have to manage the execution issues and the organisation has to have the stomach to go through the change." It is also worth remembering, says Braddock, that, "shared service centres are only part of the road map to standardised processes within a company."

The European Business Service Centre has 86 employees ranging from seasonal qualified accountants to processing clerks working on corporate consolidation, reporting, general ledger activities for the European entities, accounts payable and receivable, processing payments and ancillary SAP support.

time at its four universities and is fast becoming a target for young Europeans looking to improve their English and find employment in an area where accommodation is affordable. "The blend of UK nationals and foreign nationals is an important factor in Manchester's success," says Norwood. "SSCs in Manchester will find their staff are 40% to 60% from outside the UK and are often nationals of the country whose market they are serving. This has significant advantages when dealing with external customers and suppliers and means that a higher quality or more value-added service can be offered than from some other locations."

Cammie Seymour at Michelin agrees. Project manager at the French-owned manufacturer, Seymour has overseen the creation of the Manchester base since its inception in October 2002. "Manchester had a huge advantage in that is has a very large international population and graduates with strong language skills. We send our graduates abroad for four months at a time to learn treasury skills in another country - they have to fit in culturally but also be able to communicate," she says. The skills are then transplanted back to Manchester where Michelin employs 150 people in accounts payable, fixed asset accounting, general ledger and intra-group accounting.

CF was lucky to track down Seymour. She spends much of her time flying between Michelin's European bases to check on the treasury teams and ensure the employees are fully trained before their final return to Manchester. "We did a study over two years on whether to create a shared service centre at the European level. We looked at 15 cities in total but the shortlist came down to Manchester, Madrid or Michelin's base in Clermont-Ferrand in France."

Michelin's consultants suggested Barcelona and Lisbon, or real off-shoring locations like India. But as Seymour notes, "it's important to be in Europe as our customers are in Europe." With official corporate languages of French or English, Seymour points out that Michelin needed a destination where at least one of the

"I'm not convinced there is a pan-European SSC in eastern Europe operating on a single centre model."
Chris Norwood, MIDAS

languages was spoken. Manchester offered a good track record and an attractive cost base. "Cost was a defining factor. In Europe there is little differentiation in cost for the top-end accounting positions, but Manchester is more competitive for costs at the accountancy entry-level," she adds.

Norwood denies any competition between Manchester and other European SSCs, but with the reduced risk factor of operating in Eastern Europe today, he must recognise there is a threat to Manchester's popularity?

"If you choose between the two types of locations [western and eastern Europe] you choose between different kinds of shared service centres. At eastern European locations you have the low-cost offering but will you have the value-added aspects, such as customer relationships or infrastructure?" says Norwood, who points out that Tetra Pak, Bristol-Myers Squibb and Kellogg's already cover eastern Europe from Manchester. "An SSC in Manchester (or Rotterdam or Barcelona) will offer a wider range of languages, a wider range of professional expertise and may create value through greater efficiencies and analysis of business performance rather than simply through lower cost salaries.

"I am not convinced that there is a truly pan-European SSC in Eastern Europe operating on the single centre model that you will find is the norm in Manchester. No one is sure what's going to happen after May 1st. The drift of professionals away from Eastern Europe may actually increase the shared service centre culture in the west, and employment costs may also increase there." cf

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Glasgow's SSC scene

Scotland is shaking off its image as an industrial backwater and is promoting itself as a location for corporate shared service centres. **Jason Eden** looks at what Scotland's second city Glasgow has to offer the brave-hearted corporate.

GREATER GLASGOW & CLYDE VALLEY TOURIST BOARD

In June 2003, Glasgow was labelled the "Coolest city in the UK," by the National Geographic Traveller magazine. Now, being somewhere 'cool' may not be a priority for most corporates considering relocating their operations, but when you are trying to attract multilingual, skilled professionals to man shared service centres, it is a pretty big selling point.

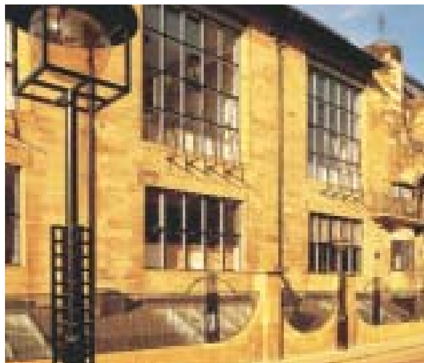
So too is a £500 million ($932 million) district purpose-built for the financial services sector with thousands of highly skilled people, 24/7 operations, dual routing telecoms and excellent international transport links.

In Scotland, traditional industries such as shipbuilding and heavy engineering have given way to IT, life sciences (the Roslin Institute in Edinburgh cloned the first mammal, Dolly the sheep), and communication technologies. Glasgow and Edinburgh have also become locations for call centres and shared service centres. One such corporate to fall for Glasgow's charms is the Eaton Corporation, an electrical power distribution company.

Eaton set up operations in Glasgow in 1997 and currently employs over 90 staff. "We looked at London, Dublin, Amsterdam and Glasgow. For us, it really wasn't a choice. Glasgow won hands down," says Jim Ward, European shared-service centre finance leader. "We thought the Amsterdam economy had too much labour inflation and London had the twin problems of affordability and retention of multi-lingual staff due to a buoyant labour market." Glasgow, says Ward, didn't suffer from these problems back in 1997, and still doesn't.

A flexible, multi-lingual labour force

Within a 20-mile radius of Glasgow's city centre there is a catchment labour force of 2.5 million people; more than 28,000 people work in the finance sector. This number is expected to increase dramatically during 2004, when the £500 million, purpose-built International Financial Services District (IFSD) is completed.



GREATER GLASGOW & CLYDE VALLEY TOURIST BOARD

Glasgow School of Art: part of Glasgow's cultural heritage

"There is a ready supply of skilled tertiary-sector labour at extremely competitive levels. This is one of the reasons why the bulk of our UK treasury service centre operations are now based in Glasgow." David Thorburn, Clydesdale Bank

"There is a ready supply of skilled tertiary-sector labour at extremely competitive levels," says David Thorburn, COO at Clydesdale Bank, part of the National Australia Group. "This is one of the reasons why the bulk of our UK treasury service centre operations are now based in Glasgow." David Smith, director of EMEA for the Scottish Development International, an investment agency, agrees: "Much of Glasgow's growth and success can be directly attributed to a flexible, stable and motivated workforce with highly developed skills for the treasury shared service centre." That Glasgow-based corporates will pay 32% less in wages than London-based companies should also be factored in.

Glasgow's financial district

The International Financial Services District (IFSD) is taking shape fast. Morgan Stanley, JPMorgan, esure and Goldfish have already moved in bringing with them over 1900 new finance sector jobs. It has been designed as a pre-equipped business area to allow fast track occupancy. There is no waiting around. If you decide that Glasgow offers everything you need from a treasury service centre, you can pretty much move in tomorrow – subject to giving notice to your current provider.

The district is actively supported by Scottish Enterprise Glasgow, and, when completed, will comprise over 20 million square feet of office space. It will also push Glasgow in to the top three cities in Europe for office availability and fifth for office value for money.

"The treasury shared service centre is already a major employer in Glasgow. We now seek to build on these strengths by creating the highest quality business environment for corporates. The competitiveness of Glasgow in the market is compounded by a cost base which is up to 40% lower than many of its main competitors," says Ron Culley, chief executive of Scottish Enterprise Glasgow.

World-class infrastructure

With the largest number of ISDN lines per capita in the UK and an extensive telecommunications infrastructure it is no surprise to find Glasgow home to BT Scotland, NTL and Thus. BT has even designated Glasgow as an eLocation, and is investing £50 million in its telecom infrastructure.

New buildings in the IFSD have dual routing – put simply, if there's a problem with one exchange, business is rerouted through the other with corporates none the wiser. "Our technical people say the telecoms infrastructure in Glasgow remains better than almost anywhere in the UK," says Eaton's Ward. But the excellent infrastructure provisions don't end at the phone lines. The IFSD offers excellent transportation links too.

Glasgow offers the largest suburban commuter rail network in the UK outside London, and boasts two major airports – Glasgow and Prestwick. "The Eaton Corporation is an $8 billion global business. Therefore, we have a number of international clients. It is extremely important for us that our European and stateside clients and personnel are able to access Glasgow easily and affordably," says Ward, who cites Glasgow's transport infrastructure as a compelling reason why Eaton Corporation chose Glasgow. With the onset of the no-frills airlines such as Easyjet and Ryanair servicing the city, flights have become even cheaper and more frequent.

So would Ward recommend Glasgow to other corporates both as a place to work and, perhaps more importantly, as a place to live? "The city is flourishing. It's a vibrant, bustling place to live. It's got something for everyone – lots of free museums, galleries, pubs and clubs, plus two major football teams." For those who perhaps don't follow Scottish football they are Celtic and Rangers. cf

SHARED SERVICE CENTRE OR OUTSOURCING?

Corporates can outsource back-office operations or create a shared service centre – the degree of control is the defining factor. But which is best for you? "There is an increasing willingness to outsource – a feeling that a shared service centre can take you to a certain point but no further," comments Alex Hamilton, at Latham & Watkins. He has identified four pressure points for corporates:

- a desire to improve reporting and risk control in treasury
- cost pressures on the back office
- increased requirements for treasury which is, in turn, struggling to grow internally
- pressure to invest in new technology

The question is a simple one. Can a corporate outsource its back-office treasury operations and then repurchase them at a lower price than it would have otherwise cost? "Companies have to create a comfort zone. There has to be a willingness to allow providers to do certain tasks." Though Hamilton admits there is an obvious corporate concern about a loss of control, it is largely a question of swapping one type of control for another.

Champagne anyone? Bumper figures for M&A growth in 2004

Any doubts surrounding the health of the global M&A market have been resoundingly dispelled by the latest batch of deal information from Dealogic. The announced volume of M&A deals so far in 2004 has reached $471 billion – this represents a whopping increase of 170.9% on corresponding 2003 figures. Given the number of announced deals – 3,274 and 3,566 for 2004 and 2003 respectively – it seems that sheer deal size is responsible for the uplift.

Goldman Sachs again leads the way in the US M&A standings, consolidating its position at the head of the pack against rivals JPMorgan and Morgan Stanley. And even though Goldman actually advised on three fewer deals for year-to-date 2004 compared to 2003, total deal volume shows an increase of 637.17%.

In the US, energy and computer industries led the way in the last week of February with the decision by TransCanada to acquire Gas Transmission Northwest from National Energy & Gas Transmission for $1.7 billion and First Data acquiring Concord for $7.1 billion.

And while America is traditionally the most vibrant M&A market it is across the Pacific in the islands of Japan that has seen the most exciting M&A news for some time. Yamanouchi Pharmaceutical announced its intention to purchase Fujisawa, its smaller Japanese rival, for around $8 billion. The deal – to be completed in April 2005 – will create Japan's second largest pharmaceutical company and may herald further M&A speculation in Japan's otherwise quiet M&A sphere.

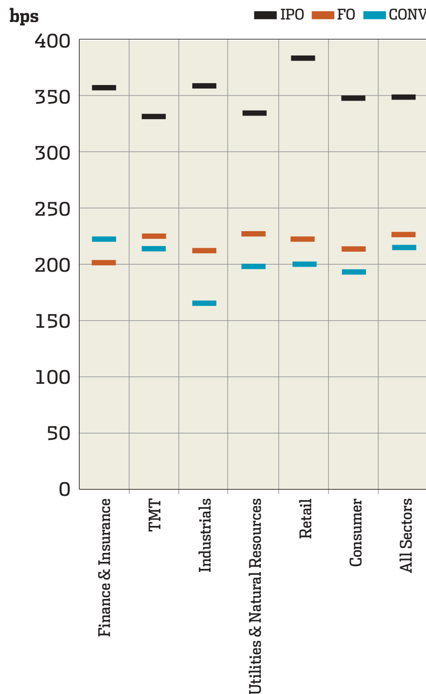
But it's not positive news everywhere. PwC's report 'Power Deals' shows 2003 as something of a nadir for the global electricity and gas markets; deal volume fell sharply from $84.9 billion in 2002 to $43 billion in 2003. The gas market, in particular, is suffering as deal values slumped from $36.3 billion in 2002 to a pitiful $3.3 billion in 2003.

TOP 10 GLOBAL M&A DEALS FEBRUARY 2004

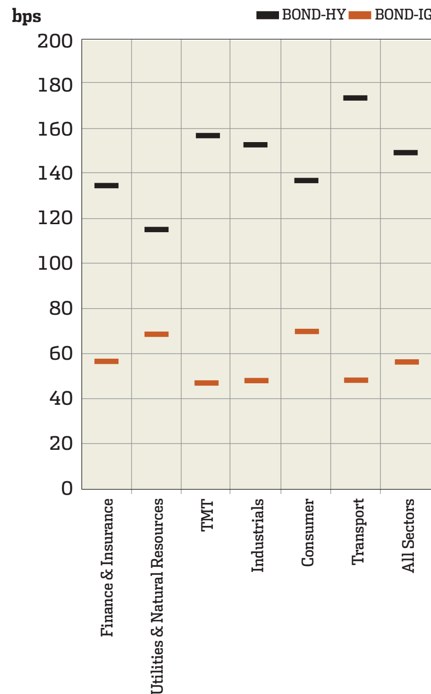
Announced	Target	Target Nationality	Target Sector	Acquiror	All Advisors	Value $(m)
11/2/04	Walt Disney Co	US	Leisure & Recreation	Comcast Corp	Goldman Sachs, Bear Stearns, JP Morgan, Morgan Stanley, Quadrangle, Rohatyn	66,603.98
17/2/04	AT&T Wireless Services Inc	US	Telecomms	Cingular Wireless	Goldman Sachs, Merrill Lynch, Lehman Bros, Evercore Ptnrs, Citigroup, JP Morgan, Rohatyn	46,770.00
5/2/04	Canary Wharf Group plc (Bid No 2)	UK	Real Estate/ Property	CWG Acquisition Ltd (IBO)	Cazenove, Deutsche Bank, Merrill Lynch, Lazard	9,699.57
24/2/04	Fujisawa Pharmaceutical Co Ltd	Japan	Healthcare	Yamanouchi Pharmaceutical Co Ltd	Lehman Brothers, Morgan Stanley	7,880.77
16/2/04	GreenPoint Financial Corp	US	Finance	North Fork Bancorp	Keefe Bruyette & Woods, Lehman Brothers, Sandler O'Neill & Partners, JP Morgan	5,671.65
23/2/04	Wanadoo SA (29.4%)	France	Computers & Electronics	France Telecom SA	ABN AMRO, BNP Paribas, Societe Generale, Morgan Stanley	4,841.15
2/2/04	Grupo Financiero BBVA Bancomer SA de CV (40.58%)	Mexico	Finance	Banco Bilbao Vizcaya Argentaria SA - BBVA	Goldman Sachs, Morgan Stanley	4,076.90
9/2/04	NetScreen Technologies Inc	US	Computers & Electronics	Juniper Networks Inc	Goldman Sachs, JP Morgan	3,504.29
19/2/04	Carlsberg Breweries A/S (40%)	Denmark	Food & Beverage	Carlsberg A/S	Goldman Sachs, Lehman Brothers, JP Morgan	3,279.02
16/2/04	Industriforvaltnings AB Kinnevik	Sweden	Finance	Invik & Co AB	Handelsbanken, Deloitte & Touche, Morgan Stanley	2,838.64

Source: Dealogic

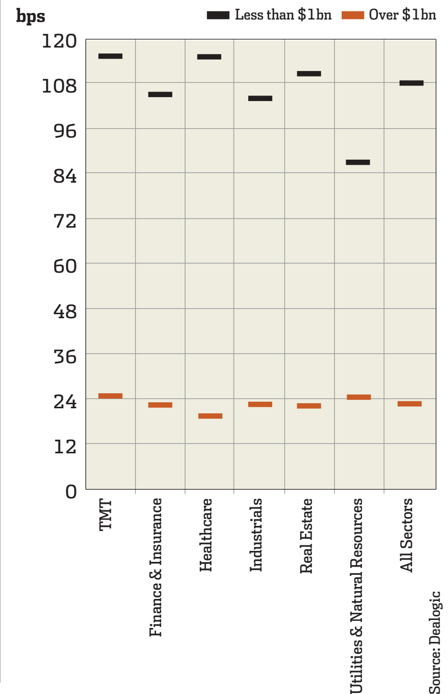
EMEA ECM SECTOR SPREADS '03 & '04 YTD



EMEA DCM SECTOR SPREADS '03 & '04 YTD



EMEA M&A SECTOR SPREADS '03 & '04 YTD



EMEA Top 5 Fee Generating ECM Deals 2003 & 2004 YTD

Pricing Date	Issue Type	Issuer	Sector	Bookrunner	Deal Value $(m)
10/04/03	FO	Allianz AG	Insurance	Deutsche Bank, Goldman Sachs, Citigroup, UBS	4,826.12
23/10/03	FO	Muenchener Rueckversiche-rungsgesellschaft AG - Munich Re	Insurance	Deutsche Bank	4,688.01
24/03/03	FO	France Telecom	Telecoms	ABN AMRO Rothschild, BNP Paribas, Groupe Credit Agricole/ Lazard, Credit Lyonnais, DB, GS, Merrill Lynch, MS	6,566.66
26/11/03	FO	Koninklijke Ahold NV	Retail	ING, Rabobank Nederland, ABN AMRO Rothschild, GS, JPM	3,384.69
20/11/2003	FO	ABB Ltd	Construction	Citigroup, CSFB, DB, Enskilda Securities	2,525.39

Source: Dealogic

EMEA Top 5 Fee Generating DCM Deals 2003 & 2004 YTD

Pricing Date	Issue Type	Issuer	Sector	Nationality	Deal Value $(m)
11/2/04	PREF	ABN AMRO Capital Funding Trust VII	Finance	Netherlands	1,800.00
26/6/03	PREF	ABN AMRO Capital Funding Trust V	Finance	Netherlands	1,250.00
29/7/03	BOND-HY	Valentia Telecommunications UPC	Telecoms	Ireland	1,213.65
2/7/03	BOND-HY	Vivendi Universal SA	Leisure	France	1,546.23
28/2/03	PREF	Endesa Capital Finance LLC	Utilities	Spain	1,621.62

Source: Dealogic

EMEA Top 5 Fee Generating M&A Deals 2003 & 2004 YTD

Announced	Target	Target Nationality	Target Sector	Acquiror	All Advisors	Deal Value $(m)
26/1/04	Aventis SA	France	Healthcare	Sanofi-Synthelabo	GS, ML, Rothschild, Citigroup, BNP Paribas, MS, UBS	68,700.39
12/3/03	Telecom Italia SpA (59.65%)	Italy	Telecoms	Olivetti SpA	GS, ML, Lazard, JPM, UniCredit Banca Mobiliare, Banca Intesa SpA	44,387.33
10/10/03	Amersham plc	UK	Healthcare	General Electric Co	Goldman Sachs, JP Morgan, Morgan Stanley	9,797.30
5/2/04	Canary Wharf Group plc (Bid No 2)	UK	Real Estate/ Property	CWG Acquisition Ltd (IBO)	Cazenove, DB, ML, Lazard	9,699.57
5/12/03	Canary Wharf Group plc (Bid No 1)	UK	Real Estate/ Property	Silvestor Holdings	Cazenove, GS, Lazard, Rothschild, MS	9,113.39

Source: Dealogic

dealogic

GLOBAL ECM RANKINGS

ECM Bookrunner Ranking Jan to Feb 2004

Rank	Bookrunner	Total Deal Value ($m)	No.	Volume Share
1	Morgan Stanley	12,004	39	13.6
2	Citigroup	9,119	44	10.3
3	Merrill Lynch	7,990	34	9.0
4	Goldman Sachs	7,661	23	8.7
5	UBS	6,100	31	6.9
6	Lehman Brothers	4,603	20	5.2
7	Deutsche Bank	4,543	22	5.1
8	JP Morgan	3,451	30	3.9
9	Credit Suisse First Boston	3,418	20	3.9
10	Nomura	3,154	36	3.6
	Grand Total	**88,471**	**798**	**100**

Source: Dealogic

ECM Net Revenue Ranking Jan to Feb 2004

Rank	Bank	Total Net Revenue ($m)	Market Share
1	Morgan Stanley	215	9.3
2	Citigroup	201	8.7
3	Goldman Sachs	182	7.9
4	Merrill Lynch	173	7.5
5	UBS	147	6.4
6	Nomura	116	5.0
7	Lehman Brothers	102	4.4
8	JP Morgan	95	4.1
9	Credit Suisse First Boston	95	4.1
10	Deutsche Bank	95	4.1
	Grand Total	**2,308**	**100**

Source: Dealogic

GLOBAL DCM RANKINGS

DCM Bookrunner Ranking Jan to Feb 2004

Rank	Bookrunner	Total Deal Value ($m)	No.	Volume Share
1	Citigroup	68,324	244	8.0
2	Deutsche Bank	58,486	299	6.8
3	Merrill Lynch	54,954	175	6.4
4	Credit Suisse First Boston	52,606	178	6.1
5	Lehman Brothers	51,288	210	6.0
6	Morgan Stanley	50,507	191	5.9
7	JP Morgan	50,267	175	5.9
8	Goldman Sachs	47,159	114	5.5
9	UBS	41,862	203	4.9
10	Barclays Capital	29,448	127	3.4
	Grand Total	**857,725**	**4,091**	**100**

Source: Dealogic

DCM Net Revenue Ranking Jan to Feb 2004

Rank	Bank	Total Net Revenue ($m)	Market Share
1	Citigroup	294	9.3
2	Credit Suisse First Boston	253	8.0
3	Morgan Stanley	207	6.6
4	Deutsche Bank	207	6.6
5	JP Morgan	182	5.8
6	UBS	173	5.5
7	Lehman Brothers	168	5.3
8	Merrill Lynch	154	4.9
9	Goldman Sachs	151	4.8
10	Banc of America	123	3.9
	Grand Total	**3,154**	**100**

Source: Dealogic

GLOBAL M&A RANKINGS

Announced M&A Adviser Ranking Jan to Feb 2004

Rank	Adviser	Deal Value ($m)	No.	Volume Share
1	Goldman Sachs	219,281	40	48.7
2	JP Morgan	199,090	37	44.2
3	Morgan Stanley	174,470	36	38.7
4	Merrill Lynch	140,696	21	31.2
5	Rohatyn	113,374	2	25.2
6	Rothschild	79,186	22	17.6
7	BNP Paribas	77,060	7	17.1
8	Citigroup	73,298	35	16.3
9	Lehman Brothers	70,278	24	15.6
10	Bear, Stearns & Co. Inc.	68,749	5	15.3
	Grand Total	**450,720**	**3,212**	**100**

Source: Dealogic

M&A Net Revenue Ranking Jan to Feb 2004

Rank	Adviser	Total Net Revenue ($m)	Market Share
1	Goldman Sachs	107	8.8
2	JP Morgan	103	8.4
3	Merrill Lynch	92	7.6
4	Citigroup	81	6.6
5	Lehman Brothers	80	6.5
6	UBS	75	6.2
7	Credit Suisse First Boston	70	5.8
8	Morgan Stanley	70	5.7
9	Deutsche Bank	57	4.7
10	Lazard	50	4.1
	Grand Total	**1,218**	**100**

Source: Dealogic

10-year benchmark long-bond yield forecasts for May 2004

	US	UK	Euroland	Japan	Switzerland
ABN Amro	4.20	4.90	4.15	1.25 ▼	---
BMO	5.00 ▲	5.40 ▲	5.00 ▲	1.90 ▲	3.40 ▲
Commerzbank	4.40	5.00	4.40	1.40	2.80
Goldman Sachs	4.20	5.00	4.50	1.40	2.70
JPMorgan Chase	---	---	---	---	---
Lloyds TSB	4.10 ▼	4.80 ▼	4.00 ▼	1.25 ▼	2.50 ▼
RBoS	4.40	5.00	4.60	1.40	2.60
Societe Generale	---	---	---	---	---
SEB Merchant Banking	4.30	4.90	4.30	1.30	2.75
UBS	4.53	5.00	4.57	1.33	2.68
Mean	4.39	5.00	4.57	1.33	2.68

Low = ▼ High = ▲

Source: Corporate Finance

10-year benchmark long-bond yield forecasts for February 2005

	US	UK	Euroland	Japan	Switzerland
ABN Amro	5.40	5.35	4.90	1.90	---
BMO	5.50 ▲	5.80 ▲	5.70 ▲	2.60 ▲	4.10 ▲
Commerzbank	5.10	5.40	4.80	1.40 ▼	3.20
Goldman Sachs	3.90 ▼	5.40	4.90	1.60	3.80
JPMorgan Chase	---	---	---	---	---
Lloyds TSB	5.00	5.30	4.90	1.70	3.50
RBoS	5.00	5.50	4.80	1.50	3.00
Societe Generale	---	---	---	---	---
SEB Merchant Banking	4.70	5.00 ▼	4.50	1.60	2.95 ▼
UBS	5.00	5.20	4.73 ▼	1.67	3.07
Mean	4.95	5.37	4.90	1.75	3.37

Low = ▼ High = ▲

Source: Corporate Finance

Three-month foreign exchange forecasts

	Euro/$	£/$	$/¥	$/CHF	Euro/£	Euro/¥	Euro/CHF
ABN Amro	---	---	---	---	---	---	---
BMO	1.28	1.83	106.00 ▲	1.22	---	---	---
Commerzbank	1.31	1.84	104.00	1.19	0.71	136.00	1.55
Goldman Sachs	1.26 ▼	1.75 ▼	105.00	1.25 ▲	0.72 ▲	132.30	1.57
JPMorgan Chase	1.33	---	101.00	1.15 ▼	0.69	134.00	1.54
Lloyds TSB	1.35 ▲	1.93	104.00	1.16	0.70	140.40 ▲	1.56
RBoS	1.31	1.88	103.00	1.20	0.70	135.00	1.57
Societe Generale	1.29	1.92	105.00	1.23	0.67 ▼	135.60	1.59 ▲
SEB Merchant Banking	1.30	1.94 ▲	100.00 ▼	1.21	0.67 ▼	130.00 ▼	1.57
UBS	1.31	1.88	104.46	1.15	0.70	137.17	1.51 ▼
Mean	1.31	1.87	103.69	1.19	0.69	135.00	1.50
Spot rate on 1 March 2004	1.24	1.87	108.95	1.27	0.67	135.59	1.58

Low = ▼ High = ▲

Source: Corporate Finance

Outback takes on greenback

Out of all the G7 members, Australia's overnight interest rate of 5.25% is by far the highest. (The six other industrial nations trail far behind with an interest rate range between 0.25% - four per cent.) This may be a factor in the rise of AUD above the 80 cent figure - a six-year highs against the dollar.

If so, there may be room for further gains. Glenn Stevens, deputy governor of the Reserve Bank of Australia, has openly stated that he sees an interest rate range between five per cent and 6.25% as being within a neutral range by today's standards. Not only does this attract further speculation of another bout of rate hikes, but also makes the AUD a hive for carry trade opportunities. Investors simply borrow from low interest rate currencies like the dollar, and hold rollover overnight positions in AUD. Admittedly you have the downside of profit-takers spoiling the free lunch, but with the state of the US current account deficit worrying analysts, and the dollar-bears shunning the currency it might just remain a profitable plan.

The reasoning behind Stevens' statement is hard to reconcile with the Australia's treasurer Peter Costello. He worries that AUD strength is not only damaging domestic exports, but hurting the economy as a whole. Perhaps that is why the Royal Bank of Australia sold AUD 1.86 billion ($1.4 billion) in January in an attempt to try and stem the rising tide. Whatever happens in the mean time, another 25 basis point rise in the differential could see the AUD smash through the 80 cent mark. **JE**

Cable hits sterling heights

Sterling hit a fresh 11-year high against the dollar in February. It climbed to the heady heights of 1.9140, a level not seen since the UK

Twelve-month foreign exchange forecasts

	Euro/$	£/$	$/¥	$/CHF	Euro/£	Euro/¥	Euro/CHF
ABN Amro	---	---	---	---	---	---	---
BMO	1.30	1.85	105.00	1.20	---	---	---
Commerzbank	1.20▼	1.74▼	110.00	1.26▲	0.69▼	132.00	1.51
Goldman Sachs	1.30	1.78	95.00▼	1.22	0.73▲	123.50▼	1.59
JPMorgan Chase	1.37	---	95.00▼	1.11	0.71	130.00	1.52
Lloyds TSB	1.30	1.83	110.00▲	1.18	0.71	143.00	1.54
RBoS	1.27	1.81	99.00	1.26▲	0.70	126.00	1.60▲
Societe Generale	1.27	1.85	104.25	1.24	0.69▼	132.40	1.56
SEB Merchant Banking	1.25	1.82	100.00	1.24	0.69▼	125.00	1.55
UBS	1.40▲	2.00▲	99.17	1.06▼	0.70	138.83▲	1.48▼
Mean	1.29	1.83	101.94	1.20	0.70	131.35	1.54
Spot rate on 1 March 2004	1.24	1.87	108.95	1.27	0.67	135.59	1.58

Low = ▼ High = ▲ Source: Corporate Finance

Forecasts for three-month interbank rates, for May 2004

	US	UK	Euroland	Japan	Switzerland
ABN Amro	1.15	4.30	2.05	0.06	---
BMO	1.25	4.30	2.20	0.10▲	0.80
Commerzbank	1.30	4.00▼	2.10	0.00▼	0.40
Goldman Sachs	1.20	4.30	2.20	0.10▲	0.70
JPMorgan Chase	---	---	---	---	---
Lloyds TSB	1.00▼	4.25	2.00▼	0.10▲	0.40
RBoS	1.10	4.40	2.10	0.10▲	0.30
Societe Generale	1.16	4.25	2.10	0.06	0.25▼
SEB Merchant Banking	1.30	4.50▲	2.20	0.10▲	0.30
UBS	1.41▲	4.26	2.25▲	0.10▲	0.86▲
Mean	1.21	4.28	2.13	0.08	0.50

Low = ▼ High = ▲ Source: Corporate Finance

Forecasts for three-month interbank rates for February 2005

	US	UK	Euroland	Japan	Switzerland
ABN Amro	2.45	3.65▼	2.15	0.05	---
BMO	2.45	4.90	3.10▲	0.60▲	1.90▲
Commerzbank	2.60	4.50	2.70	0.00▼	1.40
Goldman Sachs	1.20▼	5.20▲	3.00	0.10	1.80
JPMorgan Chase	---	---	---	---	---
Lloyds TSB	2.50	4.75	2.00▼	0.20	1.30
RBoS	2.60	4.90	2.10	0.10	0.60▼
Societe Generale	1.36	4.63	2.20	0.12	0.67
SEB Merchant Banking	2.00	5.00	2.80	0.30	0.80
UBS	2.75▲	4.70	2.37	0.10	1.25
Mean	2.21	4.69	2.49	0.17	1.21

Low = ▼ High = ▲ Source: Corporate Finance

withdrew from Europe's exchange rate mechanism in September 1992.

The high yielding currency continues to gain momentum against the dollar with many traders taking the Bank of England's (BOE) unanimous vote to raise interest rates in February as a sign that there isn't the same level of concern about currency strength at the BOE as there is at the European Central Bank.

This sentiment could not have been better for sterling, as analysts interpreted the news as allowing for further rate hikes in the next few months. Currency strategists have renewed their predictions for cable, advocating that it could hit $2 to the pound in the months ahead, as investors follow the high yield currencies and stay away from holding dollar positions. **JE**

Euro stunts growth

Let's hope the euro has a good head for heights. The European Union's basket currency hit a lifetime high of $1.2926 against the dollar in February, after yet another European Central Bank (ECB) council member waxed lyrical about the currency's pain threshold against its continuing meteoric rise. It seems the ECB's preoccupation with appropriate interest rates in the eurozone outweighs any worries it may have on the currency front.

But, Europe could well do without a strong euro. The French economy, the eurozone's second largest is struggling to grow, posting its worst growth level of the last 10 years at just 0.2 % in 2003. Germany, the eurozone's largest economy, fared even worse, contracting 0.1 % during 2003. Is it a coincidence the euro trades where it does and the largest economy in the European Union contracts for the first time since 1993?

The euro is likely to see-saw over the coming weeks as traders test the resilience of the ECB and profit-taking orders take effect on the rising currency. **JE**