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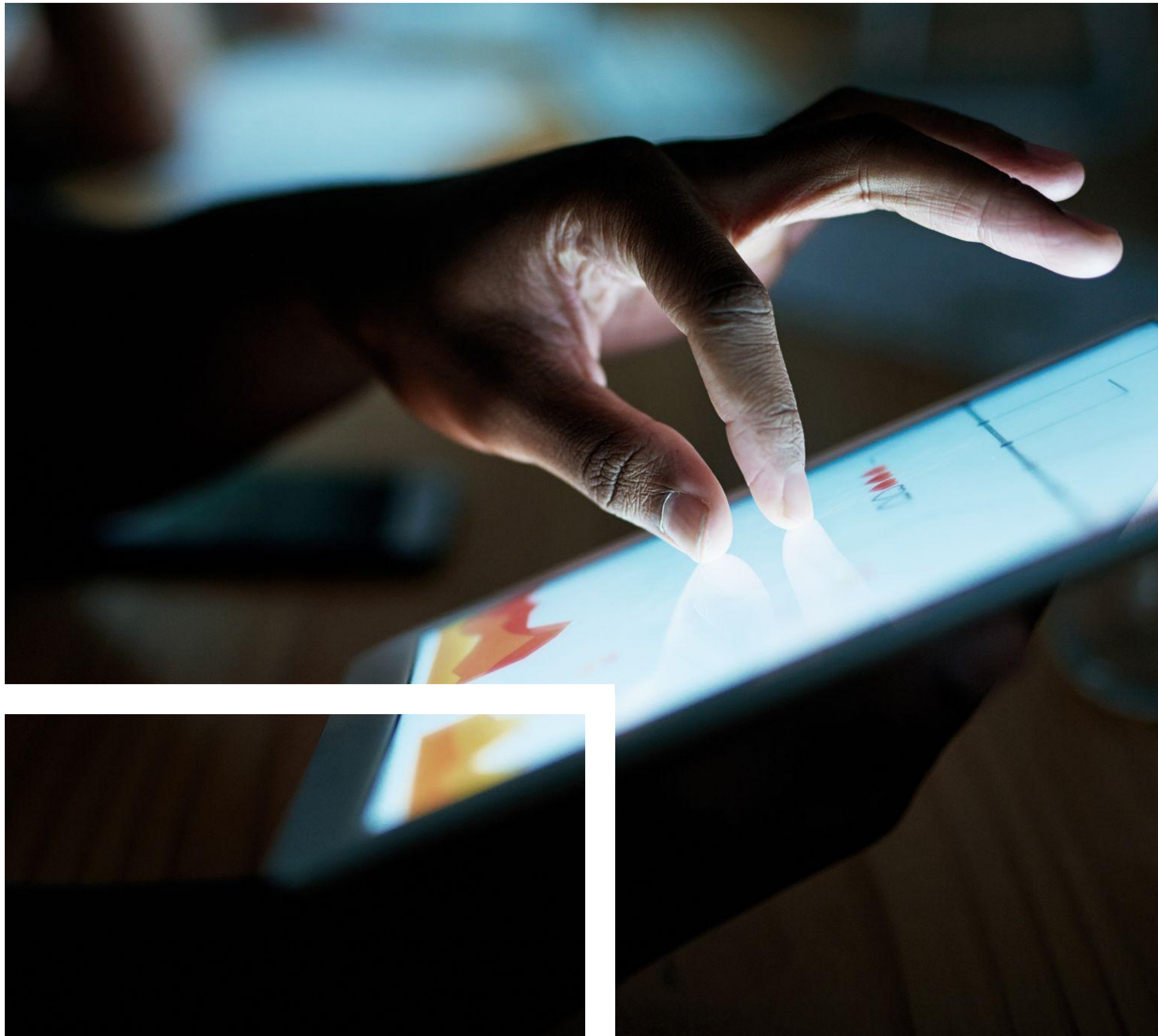
Pooling solutions today: a new way of looking at liquidity management

PwC's Survey



Document goals

The Report summarizes information gathered about the **adoption level of Cash Pooling** solutions **by Italian multinational** companies with a focus on Notional Pooling. In addition, the Report aims to understand the main **drivers** that lead companies to choose **one of these solutions over the alternatives,** highlighting the possible benefits, legal issues and physical limitations.

*In literature there exists a third type of pooling, the Virtual cash management that helps corporates manage their balances from a minimum number of accounts, while offering local subsidiaries autonomy in managing their balances on a so-called virtual ledger account.

Cash Pooling Solutions

Companies operating in several countries generally have cash balances distributed throughout different bank accounts, among several banks, in multiple currencies, and often even in different time zones. Several tools are required to manage these balances effectively; one such tool is automated Cash Pooling. These instruments are critical in enabling companies to fully control their cash balances across countries and currencies as they allow international companies to rationalize and fully centralize liquidity management operations at a regional or global level.

The basic idea behind Cash Pooling is to gain full control of cash balances and offset the debit and credit balances of all accounts in the cash pool.
There are two main categories* of Cash Pooling techniques:

Physical cash concentration	The balances of the participant's accounts are physically transferred (swept) between the sub-accounts and the Master Account of the cash pool
Notional Pooling	The balances of the participating accounts are not physically moved but mathematically combined and used to calculate interest

Snapshot of the Pooling solutions in the Italian market

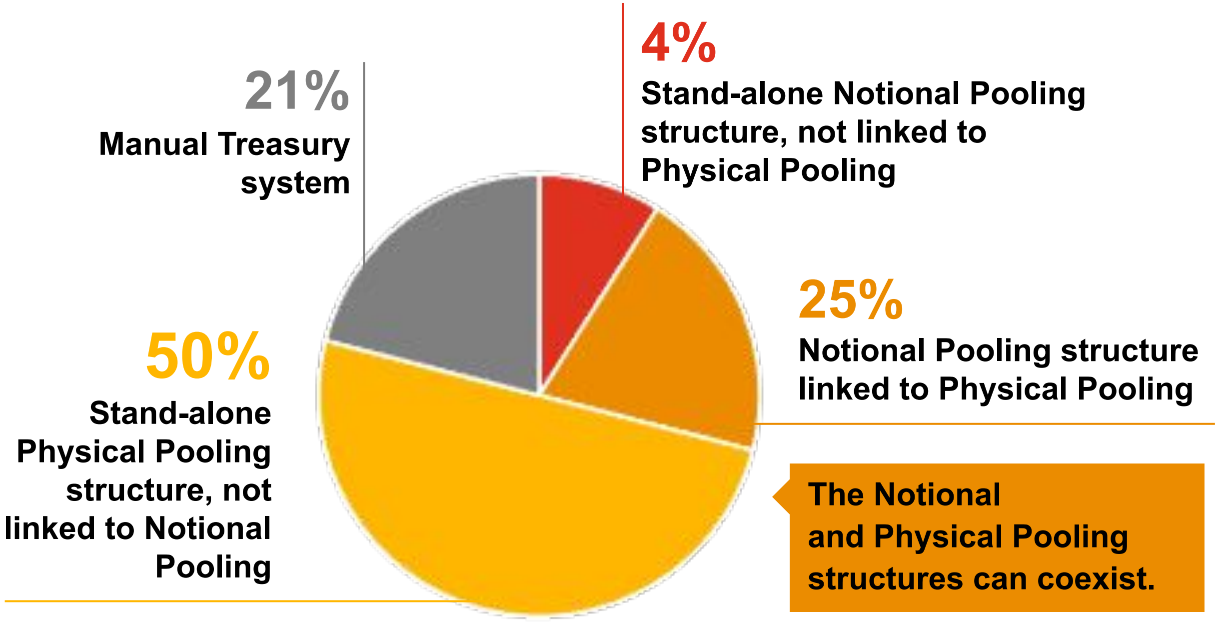
The **companies** operating in the Italian market have a **higher** and **clear preference** for a Pooling **solution** that - due to its **greater market offering** - is **perceived** as **more robust**, a comparison of the two solutions shows that the following factors are important drivers of cash pooling solution choice:

- **Number of currencies**: if companies have a limited number (e.g. only euro) of currencies to manage, the Physical Pooling solution may be sufficient; however, the Notional Pooling is very useful for more efficient and allows the management of multiple currencies.
- **Simplicity of implementation & regulation**: the Physical Pooling has a proven structure in the market, whereas the Notional Pooling entails some operational difficulties like time zones management, Treasury set-up effort, and governmental regulations.

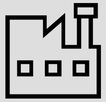
It is also possible to **combine Physical and Notional Pooling** structures to cover specific operational needs, in rare cases (4%), companies can activate **stand-alone Notional Pooling** structures to manage particular necessities (e.g. uncommon currencies).

It should be noted that there are also companies that do not have such Pooling facilities: 21% of companies interviewed adopt a **manual Treasury management system**, which is adequate for managing a few currencies and limited liquidity positions. Usually this preference for cash management applies to **smaller companies** with a **simple Treasury structures**.

What Pooling solution have you chosen for Treasury management?



The Notional and Physical Pooling structures can coexist.



63% of the companies surveyed are listed on FTSE MIB, FTSE Mid Cap, FTSE Italia Star FTSE, Small Cap and NYSE, with a combined total turnover of €173 billion.

Source: PwC elaborations base on 24 market-leading Italian companies

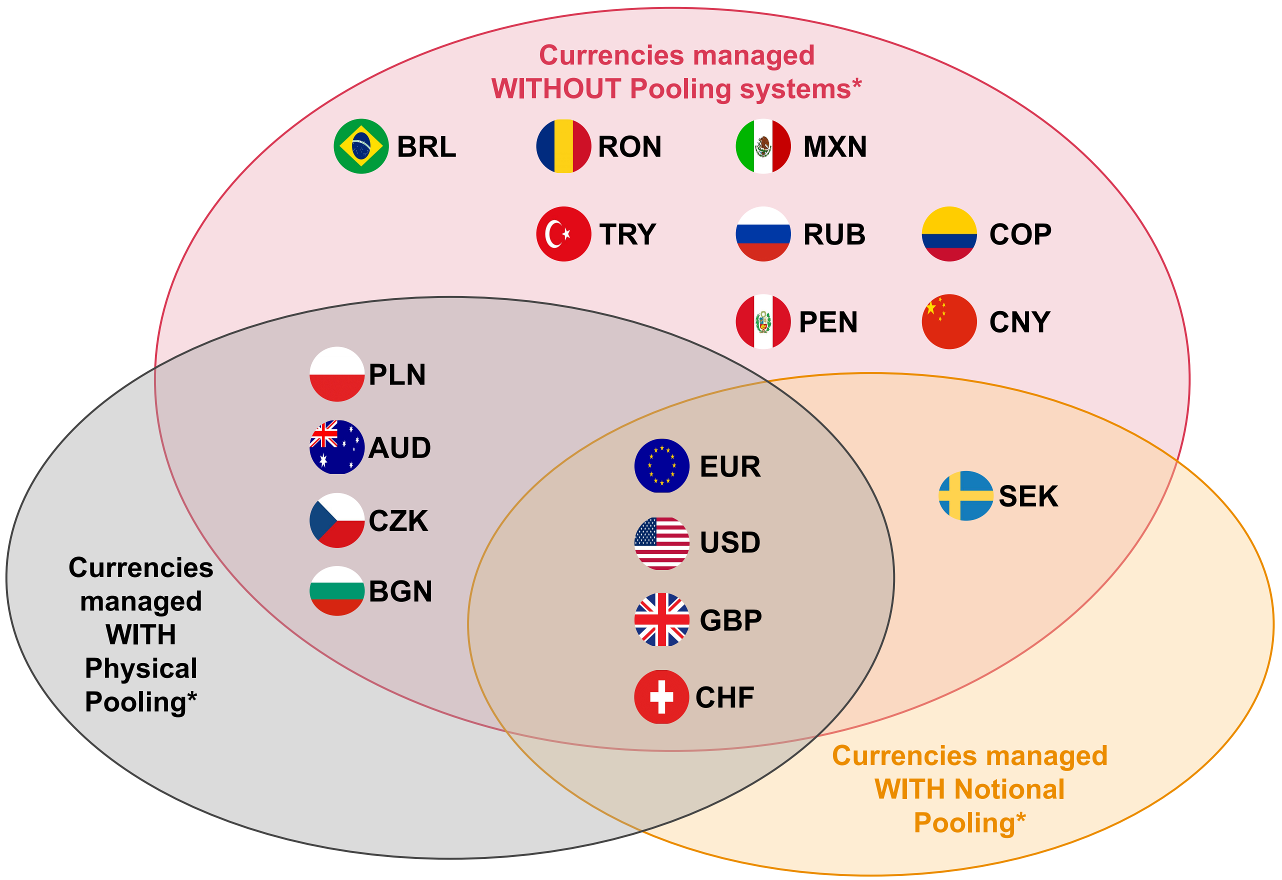
European and global currencies managed by Treasuries

The companies interviewed have a **business focus on European countries**, given their on-site presence. Therefore, after the EUR, the **most commonly managed currencies** by such companies at the international level are the **USD** and **GBP**, reflecting business operations.

Due to the **larger market size** and thus the **level of liquidity**, Pooling structures are mostly adopted for specific currencies [EUR 100%; USD 40%; GBP 35%; and rare cases of Physical Pooling with CHF and PLN (18%); AUD and CZK (6%)].

However, the **companies' operations** extend to other currencies (e.g. RON, RUB), which are **not included in Pooling** structures for two main reasons: (a) **regulatory constraints** affecting the operation of the service and (b) **restricted activity** on specific currencies.

Which currencies are managed by Treasuries?



Source: PwC elaborations base on 24 market-leading Italian companies | *List does not exhaustive

Evolutionary path: the Notional Pooling strategic relevance for corporate

The Report evidences that currently, most widely used solution of cash management is Physical Pooling but the situation could change in the near future.

Notional Pooling shows a great potential thanks to its features, such as the **multi currency management**, which is well adapted to the **evolution of the market**, which is increasingly focused on the international context.

Notional Pooling success key points

Simplifying operations

Reduction of the **operative impact** on the subsidiaries, **without loss of control** for the Pooler, by **removal of the daily zeroing** of the balances, typical of the Physical Pooling.

Capital efficiency

Combination of **credit** and **debit balances,** in different currencies, within a **single 'virtual' position** aggregated in a reference currency, potentially reducing operating costs by facing funding mismatches in payables and receivables.

Passive currencies use

Use of **liquid assets** in certain **currencies** to cover **liquidity shortages** in other currencies **without foreign exchange** transactions, decreasing the need for access to credit for “short” currencies.

Treasury operations easing

Reduction of the need to execute **frequent Forex transactions**, **diminishing** the risks of potential **exchange losses** and optimizing the rate arbitrage activities.

Easy monitoring

Unified view and **centralized management** of the liquidity and foreign exchange position, with beneficial impact on the Treasury choices.

Drivers and constraints for the Notional Pooling adoption

How **strongly** do the following **drivers impact** the implementation of Notional Pooling structures?

Main drivers	Level of impact*
Operational autonomy of subsidiaries	High
Ease of integration in ERP company systems	High
Ease of activation	Medium
Limited economic impact	Medium
Fiscal transparency	Low
Multi currency management	Low
Integration between different bank platforms	Low

Drivers takeaway

- The possibility for subsidiaries to be able to **operate independently** and not to be reliant on the holding company appears to be the main driver identified.
- Ease of **integration in ERP systems** to effectively manage the whole Treasury, controlling the liquidity position managed inside and outside the Pooling structures seems to be an important driver.

How **strongly** do the following **constraints impact** the implementation of Notional Pooling structures?

Main constraints	Level of impact*
Complexity of implementation	High
Operability limited to a single country bank	High
Service costs	Medium
No debt position within the structure	Medium
Management of different banking platforms	Low
Tax audits	Low
Cross-border payments with economic impacts	Low

Constraints takeaway

- The **risk** of **significantly complicating operations** compared to the processes currently in place is crucial for companies.
- For internationally operating companies, the limitation imposed by Notional Pooling solutions of **restricting** all **operations to a single bank** in a single country seems to be a high-impact constraint.

Source: PwC elaborations base on 24 market-leading Italian companies | * The levels of impact of drivers and constraints have been determined by considering both the number of responses for each aspect considered and the relevance attributed to them by the respondents

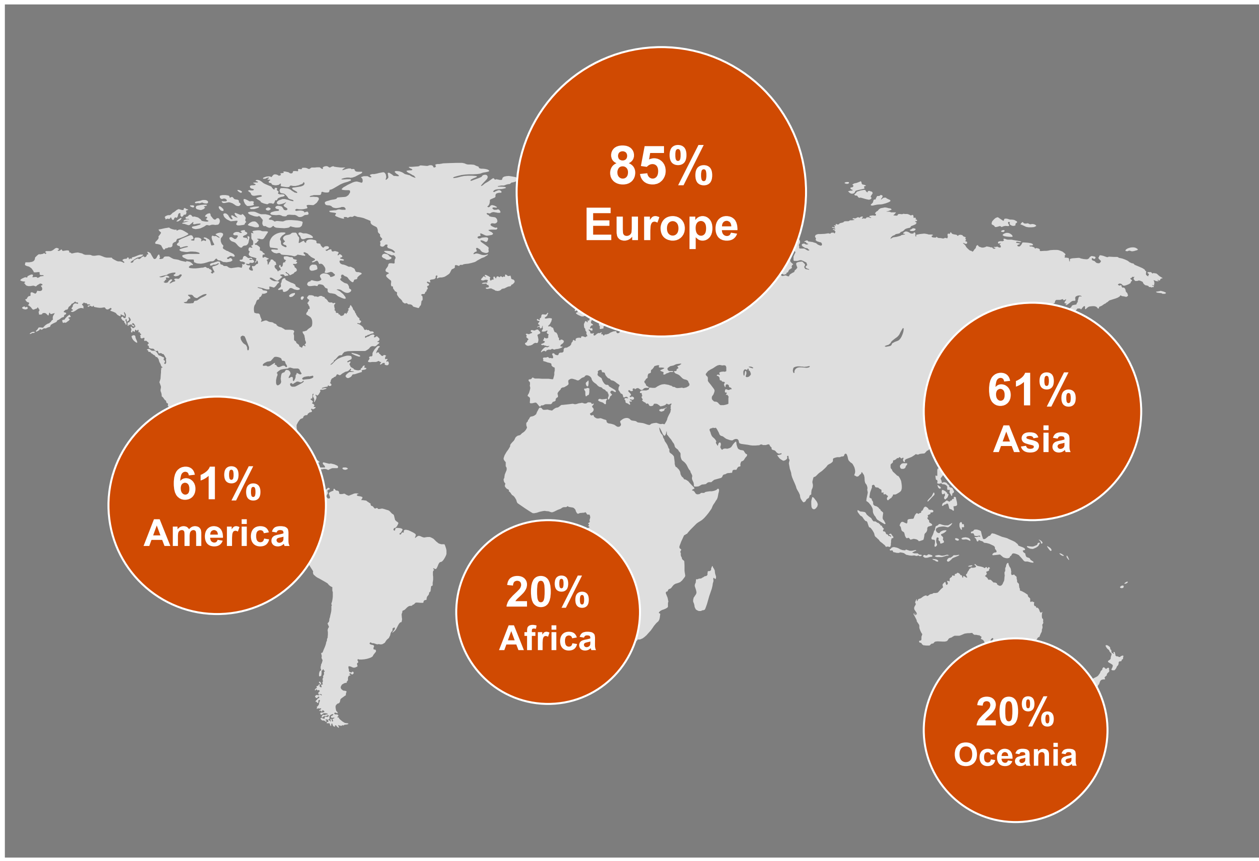
Methodological note & sample of the analysis

Sample of 24 companies, among the leading players in Italian market and operating worldwide

From € 150 million to € 90 billion of revenues

From 170 to 65.000 employees

Operating in 13 industries



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