Diploma in Treasury Management (AMCT)

Unit 3: The Treasury Manager

Exemplar

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TREASURY EXCELLENCE AS STANDARD

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Declaration

By submitting this assignment, I can confirm that the assignment content contains my own work and I give my consent for the assignment to be passed through any plagiarism detection systems as deemed necessary by the ACT.

TREASURY EXCELLENCE AS STANDARD

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INTRODUCTION

"In the current business landscape, the importance of treasury management really can't be understated" (Trade Finance Global, 2022).

The UK is currently experiencing a cost of living crisis which is especially challenging for social housing tenants. Social housing providers such as Stonewater, which has been chosen as the organisation for this project, need to manage the soaring risks associated factors such as decreased income from tenants who can no longer afford to pay rent. At the same time, costs are rising due to inflation and Stonewater needs to maintain close contact with partners to support them where we can, while protecting operating surplus and capital costs. Liquidity risk management is paramount and the treasurer will need to employ a range of skills to manage the function and team through the crisis.

Treasury cannot stand alone. The function needs to work alongside the business units to achieve the overall strategy and work cohesively to minimise enterprise wide risks. Using the tools at their disposal, such as data management and benchmarking, the treasurer needs to be agile in problem solving and project management. In times of stress, leadership is key and having clear communication can aid the team in achieving its goals.

This paper looks at the qualities and skills that are invaluable to a treasurer in terms of risk management at Stonewater and how the treasurer can effectively work with multiple stakeholders toward enterprise wide risk management.

1. THE ROLE OF TREASURY

Stonewater's vision is for everyone to have the opportunity to have a place that they can call home. The Strategic Plan for 2022-2030 sets out three main objectives to ensure that this vision is achieved (Stonewater, 2022):

1. Customer-Centred Services
2. Quality Homes and Neighbourhoods
3. Maximising Value

Key areas of risk are business risk, financial market risk (comprising market risk, liquidity risk and credit risk) and operational risk. Each business area will contribute and work towards their own risk policies and procedures, but critically, the Risk and Assurance Committee adopts an enterprise wide approach and considers risks as a collective. Even though risks are individual, they often interact and it is dangerous to consider risks in isolation. The Committee collates and monitors high scoring risks through the "strategic and critical operations risk register" (Stonewater Limited, 2022). The Annual Report and Accounts 2022 lists twelve "Key strategic risks" that the Board have identified, examples of controls in place for the management of those risks, and actions taken during the financial year to strengthen the controls (Stonewater Limited, 2022).

The Association of Corporate Treasurers ("ACT") states that the treasury function has four main responsibilities when it comes to risk management (Association of Corporate Treasurers, 2020):

1. Ensure Stonewater has sufficient cash to meet current and future liabilities
2. Identify, analyse and mitigate financial risks which could erode financial strength
3. Ensure that Business activities are funded in an appropriate and cost effective way
4. Encourage a culture of sound financial practice

The small, centralised treasury team at Stonewater acts in an agency role and behaves as a cost saving centre. With a formal feedback loop and reporting cycle, the treasury function is able to appropriately identify any areas of risk or opportunities to the business and monitor performance against those risks, contributing towards Stonewater's overall objectives.

One of the most critical tasks for treasury team is cash management. The added complexity for Stonewater historically has been its structure. Operationally, the companies are effectively meaningless as Stonewater operates as a whole. However, the treasury team not only needs to ensure that there is sufficient liquidity for the group, but also that each individual entity has sufficient access to cash as contracts are specific to certain entities. Up until March 2021, the one central treasury team was managing cash flows for nine companies.

Stonewater defines the minimum level of liquidity required at any one time to be the higher of

- contractual development cash flows for the next 18 months, or
- amount needed to retain the S&P "strong" rating for liquidity.

Stonewater benefits from an A+ long term credit rating from S&P Global (Standard & Poor's Financial Services, 2022). Treasury have a vital role in maintaining this rating in order to maximise the

creditworthiness of Stonewater and its borrowings. This high credit rating has several important financial implications for Stonewater and risk management:

1. Allows Stonewater to obtain variable rate bank funding with lower margins, implying lower interest and commitment fee payments - freeing cash to be used operationally
2. Investors require lower spreads over the benchmark interest rates, dropping the resultant cost of debt for Stonewater
3. Favourable credit terms with suppliers, freeing up working capital and aiding cash management.

A slightly unique element of funding for the sector is that most debt is secured by fixed assets (homes). Stonewater's homes are used to secure debt funding, which in turn frees up cash to build more homes, which are then used to secure further funding. A risk is the value attributed to the homes. When assigned to the lender, the value is lower than the market value of the property. There is therefore an imbalance of amount of cash that the property can contribute toward securing new debt, versus what is needed to build new homes. The homes also have to be assigned to a company. So if one entity needed new debt, but the homes were mostly in another, the first would not be able to gain the financing as it would have insufficient property collateral to secure against the debt. The valuation process with each lender takes much more time than the documentation process for the loan agreements, so security work is normally started in advance of needing debt funding to allow the team to be proactive and refinance when best (reducing refinancing risk). The Stonewater treasury team have staff who are dedicated to the management of this security pool and the valuation of the homes as it is a vital element in the funding process a critical to freeing cash up for operations.

Stonewater is risk averse. Business Planning is vital for the planning of the future viability of Stonewater. The team relies on up to date treasury forecasts and availability of reliable data. Through stress tests and simulations of the business plan, Stonewater forms its view of the nature of the liabilities which it is prepared to assume and in what proportions. In determining the optimum fixed, variable and inflation-linked mixture of debt, Stonewater considers:

- Minimising the probability of covenant breach in the short to medium term
- Circumstances where there is a non-negligible probability of a covenant breach in the medium term. Choices are to either renegotiate covenants early with lenders or to alter the business plan or funding strategy to reduce the risk. Treasury will work closely with the Business Planning and Partnering teams to adjust the plan and respective operational unit budgets
- Long term risk cannot be eliminated and can only be managed as a risk-return trade-off. The treasury team aim to mirror the fixed-floating interest rate on debt to the cost base of the company. This helps to ensure that Business activities are funded in an appropriate and cost effective way

As mentioned above, historically Stonewater has had a complex corporate structure. Stonewater is the result of a merger of two companies in 2015. Each organisation had long term debt at historically low interest rates and the collapse of the companies would have resulted in the banks renegotiating the terms. This would invariably had meant a higher cost of debt, resulting in less available cash for the business. In 2021, the treasury team persuaded the Board to collapse part of the Group into Stonewater Limited (the parent company of the Group). This collapse simplified the Group structure,

enabled the Group to optimise its property assets for security purposes, reduced complexity around accounting, audit and governance and standardised the financial covenants (Stonewater, 2022). It also helped with capital market investor relations due the structure being less complex, reduced risk and improved the resilience of the Group to one-off shocks. This was a vital stepping stone for the company's future funding arrangements. This is also a good example of where the Stonewater leadership team showed that whilst they are keen to manage risk, they were open to an opportunity when it was presented to them.

The treasury team was able to secure a further £100m of funding as a result of this streamlined structure (Stonewater, 2021). This directly contributed towards two of the three objectives of the Strategic Plan (Maximising Value and Quality Homes and Neighbourhoods). The interest rates were low and Stonewater gained access to funds to allow it to build 6,250 more homes by 2024.

2. THE SKILLS OF THE TREASURER

The ACT places problem solving into three categories: diagnostic tools, analytical tools and presentational tools (Association of Corporate Treasurers, 2022). Problems can be solved in a variety of ways and the Stonewater treasurer needs to remain receptive to various approaches in order to solve problems timeously, as the methods currently employed at the company may not be appropriate in all situations.

A feedback loop can also help a treasurer in terms of problem solving. An ordered approach can be helpful whereby one defines the potential problem, suggests possible solutions, selects the most appropriate actions and implements them. Finally, the treasurer will evaluate the success of the solution and feedback on any improvements to be made.

However, often problems do not occur in isolation and may be boundless, and a problem may arise which affects the organisation as a whole. These problems can be referred to as "wicked messy problems" (Rittel & Webber, 1973). A very recent case of a wicked messy problem arose during the sudden onset of the Covid-19 pandemic, which began in the UK in March 2020. Almost overnight, the world, and world of work, changed.

The first part of the decision-making process will likely have been to consider the timeframe that the pandemic could be in effect for. Together with other directorates, they will have needed to consider a number of short and longer-term risks and potential mitigants. A few of the very many risks that suddenly faced the treasury team were:

1. Home working only when the team had been office-based
2. Access to systems
3. Processing payments without the ability for authorisors to sign documents
4. Team management

The potential mitigants to those risks could have been (in order):

1. All members of the team already had work laptops and the team had a Business Continuity Plan ("BCP") in place that was tested regularly. Therefore, the treasury team had the equipment to work from their homes.
2. Team would need access to the Treasury Management System ("TMS"). The Stonewater TMS is cloud-based and this could be accessed from any computer in any location. Access to bank accounts for payments was also online. Access to Stonewater systems had also been tested and worked from home. While almost everything is managed through the TMS, as strong controls and compliance is in-built in to the system, Stonewater does not yet have straight-through payment processing. The TMS will generate a payment file, but this is then emailed to the payments team for them to upload and pay, after being signed on a physical copy.
3. This step had not been considered prior to the pandemic. Digital signing software was implemented quickly. Prior to this step, approvals were completed via email to ensure that controls did not fall away.
4. Team management was, and continues to be, very difficult with remote working during uncertain times. Regular catch-ups were set-up to manage workloads but also the mental health of team members during the extremely strenuous lockdown periods.

Additionally, the business was struggling as tenants, who could not work due to the lockdown, struggled to pay rent. Stonewater was unable to maintain properties with routine repairs and maintenance or conduct scheduled (non-essential) component replacements programmes. The call centre could no longer operate in the office and take tenants calls. Each of these problems needed to be addressed by various teams in turn, but they had knock-on effects for treasury.

The most fundamental risk for a treasurer to manage is liquidity risk. While the treasury team had enough liquidity for the next few years (to maintain a "strong" rating with S&P), this was predicated on the company generating rental income. The business units as a team, would have needed to recognise this increased liquidity risk and identify potential mitigants. Stonewater had established a charity called Longleigh in 2015. Stonewater was able to obtain grants and gifts from Longleigh to those residents that needed the most financial help. Stonewater was therefore fulfilling its moral obligation towards tenants, but also working towards indirectly bolstering liquidity for the company.

In the latter half of 2020, the Stonewater treasury team wanted to explore projects that could help to manage both liquidity and interest rate risk. When considering interest rate risk in an environment of rising interest rates and inflation, the team needed to be creative, proactive and flexible in finding new and efficient funding solutions. While not new to corporates, Environmental, Social and Governance-linked ("ESG") financing was relatively new to the sector and completely new to Stonewater. It would be a large, cross-directorate project that would require clear project management.

As defined by the ACT (Association of Corporate Treasurers, 2022), most projects will likely include the following stages, and this ESG project would have been no different:

- directing a project
- initiating a project
- planning
- controlling a stage

- managing product delivery
- managing stage boundaries
- closing a project

The project was managed by the Treasury team. The end goal was to have access to cheaper, alternative sources of funding, linking the funding sources to ESG. The team worked backwards, iteratively identifying the stages involved in reaching it. It was a good example of agile project management, whereby incremental steps were taken to achieve the ultimate goal. Each step of the process had its own benefits, but they also contributed to the overall aim of liquidity and interest rate management.

Step taken in this approach:

- In 2020, Stonewater became an early adopter of The Good Economy's Sustainability Standard for Social Housing, standardising ESG reporting in the sector (The ESG Social Housing Working Group, 2022).
- Treasury coordinated the production of the annual ESG reports on the back of the publication of the standard and have been producing them annually since. First audited in 2022.
- Treasury created a Sustainable Finance Framework, providing governance and controls around this new funding source.
- A £1bn euro medium-term note programme ("EMTN") was established to help meet Stonewater's key targets and strategies to reduce net carbon emissions and support Stonewater's social impact. It would give treasury the platform to be opportunistic in accessing the debt market with little notice.
- Opportunistically issued first sustainability-linked benchmark £250m bond from this programme in September 2021 (Stonewater, 2021).

Because the treasury manager thought ahead and prepared the programme, Stonewater was able to access this opportunistic funding which has proved vital considering the markets in mid-2022. Stonewater has now also established ESG-linked revolving credit facilities ("RCFs") to allow for the potential upside of margin decreases should Stonewater achieve a prescribed set of ESG key performance indicators ("KPIs"). While the RCFs themselves are vanilla, the treasurer explored ways to enhance them to minimise interest rate risk further.

All of the tasks above were mini projects in themselves, but there were a manageable number of them. Gantt charts can prove useful tools in project managing projects of this scale as they diagrammatically show milestones and timelines and can be invaluable for resource management. Project management software could be considered, but this particular project was arguably too small to justify it.

Ultimately the project will have been reviewed (completing the feedback loop) against costs, time (Gantt chart also helpful here) and quality to evaluate the success of the project. This learning can be used ahead of beginning new projects going forward.

3. BENCHMARKING AND DATA MANAGEMENT

Benchmarking is a critical part of the feedback loop. Benchmarking is understood to be the comparison of the performance versus a recognised standard.

Stonewater maintains a formal counterparty risk policy in respect of those organisations from which it draws funds on committed facilities, enters into derivative transactions or deposits funds with. The longer the maturity of the commitment period, derivative or investment, the greater the counterparty credit risk, and hence the minimum credit quality requirements will be more stringent.

In the world of social housing, benchmarking versus peers can be difficult for the treasurer as information is not always readily available. The associations are not listed, so the treasurer cannot look at analyses from research analysts. However, a lot of information for benchmarking requirements can be found in peer's annual accounts.

A useful source of peer information is the Treasury Managers Group ("TMG"), which was set up by treasurers in the sector to facilitate open dialogue via regular calls and meetings. There is an aspect of competition from an operational perspective in the sector, but less so from a treasury perspective, so managers are open and honest in this group. This resource is invaluable for a social housing treasurer for benchmarking. Recently it facilitated discussions regarding performance of a particularly prevalent English bank. All treasurers took a collective position with regards to monitoring the performance of its service. Auditors are compared and financial covenant definitions are often discussed. This final point in particular has been a helpful source for benchmarking Stonewater's own covenants. Many housing associations are struggling with interest cover levels, with many lenders still deducting MRI from operating surplus (capitalised repairs and improvement expenditure), which worsens interest cover. For context, it is worth noting that housing associations have been mandated by the government to spend more on homes to ensure that they meet a minimum EPC level C by 2030. (Department for Business, Energy & Industrial Strategy, 2018). Most housing associations have been told that the banks will not move on this point. However, the same banks have excluded it from the definitions for other associations. This benchmarking gives the treasurer some confidence to stand firm in future covenant negotiations with lenders.

Benchmarking for the treasury team is most often used when securing new funding. There is always an element of pricing risk and Stonewater relies on its advisors for their expertise on timing and prices achieved for other similar associations. Advisors will have a good understanding of current and fair margin levels that Stonewater could expect to achieve on variable rate bank lending (i.e. margin of interest over benchmark rates like SONIA). This knowledge can prepare a treasurer for discussions with lending banks when looking at new financing, therefore reducing pricing risk. The levels of debt in the sector are high, so movements in pricing will have severe effects on Stonewater's cost of funding. While not always publically available, banks and advisors will have information regarding the spreads achieved for other associations with a similar credit rating. Or indeed, spreads achieved for associations with better or worse ratings. Stonewater uses this information for two purposes:

1. Assessing the cost of funds that could be achievable if Stonewater went to market
2. Assessing the impact of a credit rating downgrade or upgrade on future cost of funds.

As discussed in THE ROLE OF TREASURY, Stonewater defines the minimum level of liquidity that it is willing to accept as the amount needed to retain the S&P "strong" rating. This measurement is used in the business plan and various stress-testing scenarios to ensure that Stonewater always has enough liquidity to maintain its credit rating.

KPIs can be used to measure risk and often treasurers are given KPI targets in order to manage risk levels. KPIs can be benchmarked against historical or forecast performance and can be a good indicator for the treasury team of the direction of travel of that particular risk. A worsening KPI can be a trigger for the treasury team to take action.

In today's fast-moving world, Stonewater cannot wait for data to be captured and analysed. Organisations like Stonewater are under pressure to be able to respond and adapt quickly to changes in the markets and economic environment (Bruno, 2014). Data management is critical, both to Stonewater and its treasury team. The ACT sited The Economist in saying that there are several drivers for treasury teams becoming for data-centric, such as:

- Improved operational efficiency
- Improved returns on investments
- Improved risk management
- Improved ability to influence Stonewater's strategy
- Reduced costs
- Improved forecasting
- Identifying opportunities for Stonewater

Spreadsheet models, while useful, are often built by one person or team, and therefore only truly understood by that person or team. This in itself poses a risk were that person to leave Stonewater. The treasury team (and most teams at Stonewater) needs to produce timely, accurate and reliable reporting of data. Specialist data management software, like a TMS, can overcome these particular risks. Considering Stonewater's structure of seven companies, a TMS is vital for the management of the individual loan books, investments and payments from those companies. A TMS contributes towards the reduction of two types of operational risk, error and fraud.

Stonewater holds a lot of personal data of its tenants and this information is subject to General Data Protection Regulation ("GDPR"). The management of this sensitive data is of such a high importance, that all Stonewater colleagues, regardless of their role, undergo compulsory data management training at least annually. Stonewater places so much import on this facet of work, that it recently appointed a new Chief Information and Transformation Officer (Stonewater, 2022) who will be responsible for technology and data.

There have been two cases of cyber-crime recently that have rocked the sector. Clarion, the UK's largest housing association, was a victim of a major cyberattack in June 2022. The attack affected phone lines, services and access of the company to all data regarding its own assets and those of its tenants. Social Housing reported that Clarion had announced ""extensive damage" to its IT systems and had warned that it was facing a "long period of disruption"" (Wilmore, 2022). Inside Housing reported that months after the attack, residents were still feeling anxious and ignored (CUFFE, 2022). It will likely face a credit rating downgrade and has suffered a huge reputational blow. The second

case was that of Bromford Housing Association who suffered a cyber-attack in July 2022. However, the BBC reported that the attack had been unsuccessful (BBC, 2022).

In the wake of the war in Russia-Ukraine and the increased threat of cyber-crime, cemented by the attacks on both Clarion and Bromford, Stonewater proactively sought the advice of an internal auditor for BCP and data management purposes. All teams now have robust data management and BCP plans in place. The Stonewater TMS is cloud-based with multi-factor authentication for accessing the data. This way, the treasury team have secured their data and will have access to it from any location.

Data management is key to the Stonewater treasury team and has allowed it capacity to explore new funding opportunities and products which it would not have had the capacity to do without the TMS.

4. LEADING THE TREASURY TEAM

An effective treasury leader is able to lead their team, but also effectively lead themselves. This self-awareness is an invaluable tool to a leader in terms of how they approach leading their teams. Bruce Daisley wrote in his book, The Joy of Work, that "nothing affects what we think about our job more than our relationship with our boss", and that people "resign from their managers, not their job". (Daisley, 2020). One element of risk management that this paper has not yet addressed in that of personnel. It is also no. 10 in Stonewater's Key Strategic Risks (Stonewater Limited, 2022). The relevance is the retention of staff and is where the leadership of the treasury team plays a vital role.

A motivated team will be driven, happy and more likely to work hard and perform well (BBC, 2022).

Learning can be an effective motivator. In 1984, David Kolb devised a concept called Experiential Learning Theory. It was a four stage cycle of learning, centred on experiencing, reflecting, thinking and acting (McLeod, 2017). This method has been proven to be effective as it diverges from previous methods where leaders simply transmit, but actively engage and allow their teams to learn with action.

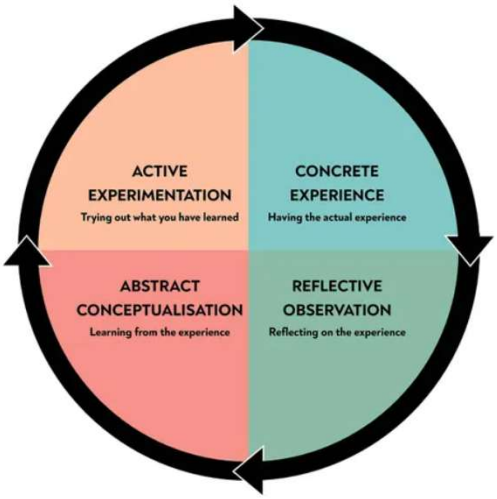


Figure 1: Kolb's Experiential Learning Cycle

Effective treasury leaders should promote diversity of thought. Without it, the team runs the risk of falling into to a pattern called "group think", as termed by Irving Janis in 1972. He suggested that group think is where groups of people begin to behave and think in the same way, with the same values. While it appears logical to the group, it may not appear so to an outsider. Without diversity of thought, the treasury function runs the risk of stagnation. The team will not be able to effectively work toward risk management if it is blinkered to all types of risk and opportunity. An effective treasury leader should be able to identify when they think that group think may be occurring and find ways to address it. The Johari model is a psychological tool which was coined by Joseph Luft and Harry Ingham as a tool for understanding and training (Luft & Ingham, 1955). It helps to understand conscious and unconscious bias within ourselves and helps to better understand your

team members. What it effectively promotes is team members getting to know each other on a deeper level, a greater self-awareness of the individuals, accepting each member for who they are and what they represent and thus minimizing the risk of group think in the team. One extra element that an effective leader can introduce is a feeling of a “safe space” where team members feel empowered to vocalise ideas and opinions. This freeing of thought and self in the team promotes acceptance and allows the individuals to think in news ways. This allows them to function and work as the best version of themselves. Stonewater proudly celebrates diversity is working hard to create an inclusive culture that allows all colleagues to grow, develop and succeed. It is focused on ensuring that colleagues feel like they belong, feel valued, and have a voice. This ambition helps to combat group think and will help attract and retain the best talent.

Victor Vroom’s Expectancy Theory (Vroom, 1964), suggested that if a person worked harder, that they would perform better and that this work would be rewarded. He went further to say that if a leader provided the appropriate resources, skills and support, the team member will thrive. The treasury leader should aim to promoting continuous professional development (“CPD”) to stay up to date with developments in the treasury field. Stonewater actively encourage CPD and have Leadership Programs in-house to promote the next generation of leaders.

Part of the success of the treasury leader is of course their ability to lead. However, it is also important to have a team of capable and loyal followers. Stephen Lundin and Lynne Lancaster suggested that the art of followership will be just as important as leadership in tapping into the potential of your teams (Lundin & Lancaster, 1990). If a treasurer can effectively lead a team of knowledgeable followers, then the productivity of their team can truly be tapped.

Stakeholder management, both internally and externally is a key part of a treasurers job. Key internal stakeholders at Stonewater would be the Finance Challenge and Assurance Panel (a Board sub-committee), the Development team (the main commercial team) and the financial reporting and business planning teams. Externally, relationships need to be built with advisors, lenders, banks, ratings agencies and regulators, to name a few.

Over the past 3 years the treasury team at Stonewater have worked to increase their profile within the organisation. While the function can sometimes appear to simply work behind the scenes, the work that the team does is critical to operations. The internal relationship that has improved the most is that with the Development team. Historically, their cash flows have not been reliable, making cash flow management for the treasury team near impossible. Over time, via productive meetings with members of the team both up and down the hierarchy, the treasury team have been able to make the relationship work for both parties. The key part of the relationship was explaining that Stonewater is one team and that treasury are here to help make funds available for the business units to effectively do their jobs.

The key external stakeholders for Stonewater are its bank lenders and credit rating agencies. As of March 2022, c. 30% of external debt was bank funded (Stonewater Limited, 2022), all with associated financial covenants. A large task for the treasury team was the renegotiation of the banking facilities and covenants in the restructure of 2021. Long-term relationships meant that the lenders understood the rationale for the company restructure and were able to easily support it when approaching their credit committees.

Stonewater's lawyers are an essential stakeholder. While they are paid to provide a service, a solid working relationship and mutual respect allows for Stonewater and the legal teams to work effectively and collaboratively to minimize the risks of clauses being missed or overlooked in agreements.

Credit rating agency relationships are vital, as described in THE ROLE OF TREASURY above. Being able to effectively communicate and showcase Stonewater's viability can mean the difference between a rating movement or not. This in turn has a cascading effect on the company's reputation and cost of funds.

For both team leadership and stakeholder management, Matthew Rose at Royal Mail said it very well in The Treasurer (2015), "The secret to success…is having the professional and personal skills to be able to effectively 'influence and negotiate with both internal and external parties'".

5. NEGOTIATION AND COMMUNICATION

Conflict is inevitable in a Treasurer's career and can often be healthy. In the previous chapter we discussed the concept of group think. If a team, or organisation is displaying symptoms of group think, conflict is unlikely to arise. However, if the team and organisation has been resourced with a diverse range of employees, conflict is inevitable. It can lead to innovative idea solutions that none of the parties had originally foreseen. So conflict, if managed well, can drive change and innovation.

However, more often than not, conflict is the result of a disconnect between parties in terms of values or ideas. This is where the skills of clear communication and tactful negotiation are essential, to de-escalate and resolve conflict.

The treasurer is constantly participating in some form of negotiation. They could be with lenders regarding covenants, levels of service or terms of loans. They could also be in the context of Merger and Acquisition ("M&A") deals, around pricing or expectations, to name a few. Internally, they could be with other departments or even within the Finance department in terms of working and resourcing to achieve joint goals.

The ACT suggests that there are four key types of conflict (Association of Corporate Treasurers, 2022):

1. interpersonal
2. intragroup
3. intergroup
4. interorganisational

Each one will affect the Treasurer at Stonewater, at different times. As mentioned in THE ROLE OF TREASURY, while working closely with the Business Planning team, if a breach of financial covenants looked remotely possible in the medium term, the most appropriate course of action would be to alter the Business Plan, rather than renegotiate covenants with lenders. To do this, each operational business unit would need to alter their forecasts, which could affect their strategy and the company's strategy overall. While the goal is absolute and non-negotiable, as breaching covenants is at the top of the risk register, it can be frustrating for the business units who have worked hard on their budgets and forecasts in an attempt to reach their own team goals and to align with corporate strategy. The

treasury team at Stonewater have built up a reputation of hard work and excellence and this has afforded it a certain level of respect and trust in the organisation, which aids stressful negotiations like these.

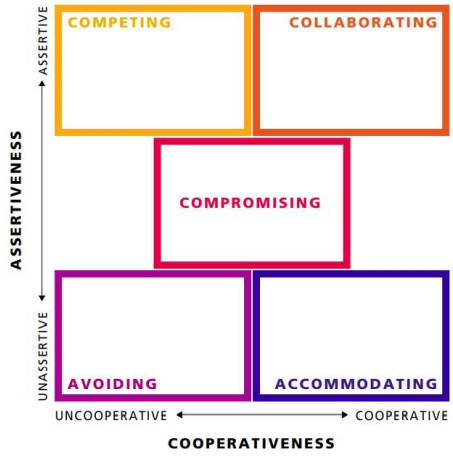


Figure 2 Adaption of Thomas' conflict management grid

Kenneth Thomas devised a conflict management grid that comprised of five management styles (Thomas, 1976) (Figure 2). The ideal goal in this model is collaboration, which is a scenario whereby both sides win. In order to reach this solution, both sides require high levels of empathy (or cooperativeness) and assertiveness. In a perfect world, the treasurer collaborate with the operational units to find a solution that suits both sides. These negotiations begin to break down when either both sides are uncooperative and lacking assertion, this avoiding the problem and running the risk of a covenant breach. Or if teams are too combative or accommodating. It is a fine balance and one which requires early and clear communication.

A recent example of where the treasurer at Stonewater will have needed to display negotiation skills has been during the current cost of living crisis that is affecting the United Kingdom ("UK"). The Office for National Statistics reported that the Consumer Prices Index ("CPI") rose by 10.1% in the 12 months to September 2022 (Office for National Statistics, 2022). Food inflation rose to a record high of 11.6% in October 2022 (Taaffe-Maguire, 2022). The BBC reported that inflation has driven the fastest fall in real pay since records began, with wages growing by 4.7% from April to June 2022 (BBC, 2022). The risk to Stonewater is the inability to retain staff as wages inevitably struggle to keep up with inflation levels. From Stonewater's perspective, investors are expecting to see ambitious development programs for new homes. As noted above, it has been mandated by the government to spend more on its homes to ensure that they meet a minimum EPC level C by 2030 (Department for Business, Energy & Industrial Strategy, 2018). However, the government is also expected to announce a rent cap in November 2022, which will force Stonewater to cap the increase in rent for its homes at a certain level. This tension is putting real pressure on housing associations, especially with respect to interest cover levels. With this context the treasurer will need clear messages from the chief financial officer ("CFO") and Board with regards to employee pay and job security. The result of these discussions will certainly impact the ability of the team to deliver an optimal service to the business.

In June 2022, Stonewater announced its intention to merge with Greenoak Housing Association ("Greenoak") (Stonewater, 2022). The two associations are incredibly different in terms of size and culture. Stonewater owns and manages c. 35,000 homes, whereas Greenoak owns and manages c. 550 homes. Stonewater has over 800 employees and has embraced technology and hybrid working, Greenoak has less than 20 employees and work is largely manual. However, there are huge synergies to be gained by both associations as a result of the merger.

The innovative change in the treasury function in this case is moving from manual excel models and payments, to working with a TMS. When Stonewater adopted their TMS in 2017, similar issues arose to those that are sure to arise in the proposed merger with Greenoak.

Examples of areas of concern or conflict with this particular change in the treasury function:

- Greenoak's manual method of work has worked up until now. Why is the change necessary
- A lot of work is required, above and beyond someone's day job, to move to the TMS and to conduct testing; and
- Once using the TMS, employees may assume that there is no use for their role

These conflict points, the final one in particular, are highly personal and emotive. Interpreted in the wrong way, they could be seen to imply that the team has been doing a suboptimal job and that their roles are no longer of use. The key goal for the Stonewater treasurer would be to convince the Greenoak team of the significant benefits of a TMS in terms of risk management, enforcement of segregation of duties and freeing up time of staff to work on innovative and creative tasks. Transparency and trust, key elements of the ACT's Code of Ethics, are crucial attributes that treasurers on both sides will need to master to progress the negotiations. The treasury team could also consider a list of minor concessions which could make a large difference to the perspective of Greenoak and could progress discussions on Stonewater's list of non-negotiables.

This potential merger will involve teamwork with all directorates at Stonewater, as well as with Greenoak. Openness of discussion will allow all teams to identify and evaluate the risks associated with the potential transaction. Key skills that the Stonewater treasurer will need to master in these merger negotiations will be listening, understanding others (both at Stonewater and at Greenoak) and a resolve to walk away from the merger if negotiations break down.

CONCLUSION

Treasury has a vital role to play in risk management for Stonewater. It cannot only consider the immediate risks to treasury, but must consider the wider picture and contribute toward enterprise-wide risk management. In order to effectively obtain this objective, the treasurer needs to be agile in their ability to problem solve and tackle often "wicked messy problems" in an ordered way. Perhaps in order to solve one larger problem, such as operating during the Covid-19 pandemic, several other smaller risks and problems need to first be addressed.

Benchmarking is a useful tool for treasurers, but it is not always easy to do. Sometimes benchmarking information can come from alternate sources, such as the TMG, and the treasurer needs to be receptive to these less conventional sources of data. A TMS is vital for data management, especially considering the size of the Stonewater treasury team and the complexity of the corporate structure.

Ultimately, the treasurer would not be able to manage risk for the function without effective leadership and communication skills. A strong leader can bring out the very best in their teams, whereas a weak one will break a team apart. Often, managing risks can mean difficult conversations with other business units, and strong negotiation skills of the treasurer can result in effective collaboration where both sides feel like they have won.

Risk management is an ever-evolving task and only effective treasury leaders will be able to navigate themselves, their teams and their organisations through periods of adversity.

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APPENDICES

Appendix 1: Organisation Background Information

Name of organisation:

Stonewater.

Type of organisation:

Housing Association.

Main products/services:

Stonewater is a social housing provider, aiming to provide homes to people in England whose needs cannot be met by the open market. Stonewater provides home for residents to buy, rent or jointly share in the ownership thereof. The company builds, acquires and jointly manages homes in England.

Size of organisation:

Stonewater employs over 800 people in the UK. In the financial year 2021/22 it had a turnover of £225m and £2.2bn of fixed assets. (Stonewater Limited, 2022)

Main operational locations:

Stonewater operates nationally, across England. There is no presence in London.

Main customer markets:

People in England most in need of affordable housing. This includes specialist accommodation for vulnerable and elderly residents, victims fleeing domestic abuse, LGBTQ+ safe spaces and young peoples' foyers.

Main supply markets:

The construction industry in relation to Stonewater's construction of new, affordable homes. Local Authority partners for joint management of properties. Repairs and maintenance service industry for the continual maintenance of homes. Utility companies for utility supple to communal spaces.

Financial reporting currency:

GBP.

Treasury structure:

The treasury team functions in an agency capacity and the structure is centralised. The function's response to risk is that of a cost saving centre.

Any other relevant information:

Stonewater is a Registered Provider. The industry is heavily regulated by the Regulator of Social Housing, as set out in the Housing and Regeneration Act 2008.

Selected theme:

Theme One – Risk Management

Relevance of selected theme:

Stonewater is regulated by the government and is regularly assessed in terms of its Governance, but also its Financial Viability and ability to mitigate its exposures effectively. The sector is predominantly financed through very high levels of debt, with levels forecast to rise as costs continue to soar. The company is a not-for-profit, so all profits are put back in to operations. The government can dictate the rate at which rents can be inflated, thus curbed income. The government has also mandated that homes meet EPC level C by 2030 for all social housing landlords (Department for Business, Energy & Industrial Strategy, 2018). The industry is balancing spending more to reach this target, while managing lower income. Financial covenants are getting tighter as a result and associated risk management is becoming ever more critical.

Operationally, especially since the Grenfell Tower tragedy of 2017, there are significant health and safety risks associated with the properties that Stonewater owns and manages. The Building Safety Act 2022 formalised building safety legislation with the largest leap in building safety regulation in the industry for many years.

(430 words)