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# Annual Conference

OCTOBER 27-30, 2013 | LAS VEGAS

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## Global Liquidity Management

### Increasing Liquidity Through Efficient Global Treasury Structures

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# Treasury Priorities...



...based on Citi Treasury Diagnostics research.

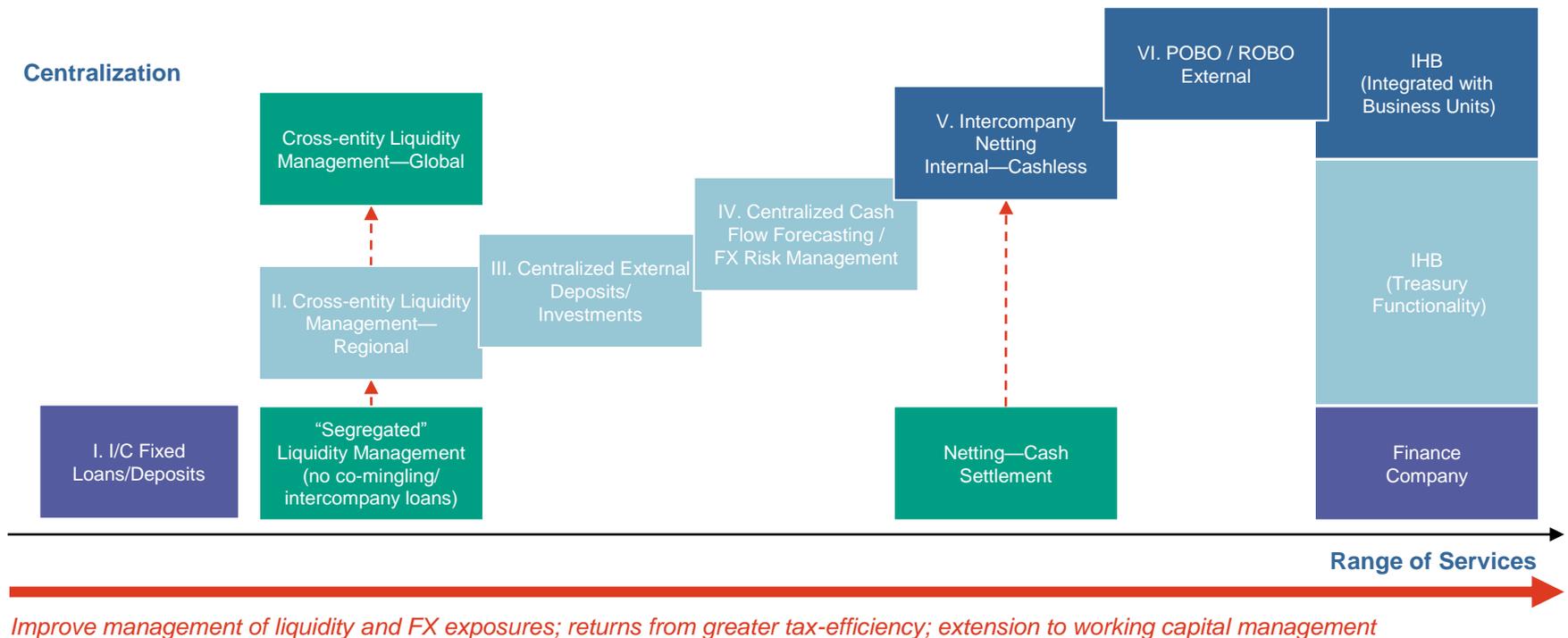
- 1 Re-organize treasury structures for continued business growth in emerging markets
- 2 Optimize working capital funding strategies for subsidiaries, especially in regulated markets
- 3 Globalize operating liquidity management, including IHB models, to release excess cash
- 4 Prepare for financial regulatory (e.g. D-F), market infrastructure (e.g., SEPA) impacts
- 5 Leverage regulatory changes in key emerging markets (e.g., China)
- 6 Leverage converging banking industry standards and corporate systems investment

		Trends				
		Macro	Regulatory	Technology		
Treasury Impacts	Governance	1	4	3		
	Structure	1	4	5	3	6
	Cash & Funding	2	4	5	3	
	Risk				3	
	Systems				3	6

# Treasury Efficiency Constructs: In-House Banks



An IHB is an evolutionary process that includes numerous functional areas. The defining aspect is whether there is an aggregation of (some or all) liquidity and risks through a legal entity that faces off with external banks.



## Some factors driving a company’s placement along IHB continuum

- Treasury Organizational Structure
- Technology
- Business Operating Model
- Regulatory and Tax Considerations

# In-House Bank Benefits



An IHB reduces FX and cash transactions, improves net interest, and increases control from centralization.

## Liquidity Management Benefits

### Centralized Investment

- Higher return from investing surplus cash in larger quantum or for longer tenor
- IHB earns a return on investment higher than the interest it pays on deposits received

### Intercompany Funding

- IHB earns spread between deposit-taking and lending among participants
- Use of virtual accounts to record participant positions minimizes subsidiary-level external bank accounts
- Simplified cash flows
  - Reduced volume of external financial and cash transactions, bank charges
  - Fewer reconciliations

## FX Management Benefits

### Netting

- IHB nets FX transactions (of the same currency pair) between subsidiaries, reducing volume and cost of FX transactions with external banks while earning a spread
- Netting lowers the volume of same-currency pair spot FX transactions, reducing transaction fees and processing errors
- IHB profits from quoting a larger bid-ask spread to participants than what it receives from external bank (transfer pricing needs to be justified)

## Subsidiary Funding and Repatriation Benefits

### Subsidiary Capital Structure

- IHB may offer an efficient vehicle for optimization (e.g. conversion of equity at subsidiaries to debt in form of IHB loans)
- Retained earnings are repatriated (where feasible and practical) and replaced with LT debt from the IHB, within country thin cap limits to allow tax deductibility of interest

Note: Jurisdictions with limitations on currency transferability and/or convertibility restrict achievable benefits.

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## Case Study: Warner Music Group (WMG)

# Warner Music Group Overview



## Recorded Music



## Music Publishing



<b>Product</b>	<ul style="list-style-type: none"> <li>Recordings</li> </ul>	<ul style="list-style-type: none"> <li>Songs/Compositions</li> </ul>
<b>Artists</b>	<ul style="list-style-type: none"> <li>Recording Artists</li> </ul>	<ul style="list-style-type: none"> <li>Songwriters/Composers</li> </ul>
<b>Source of Revenue</b>	<ul style="list-style-type: none"> <li>Physical CDs</li> <li>Digital downloads, streaming, cloud services</li> <li>Expanded Rights: Merchandising, branding touring/ticketing, film, TV, advertising</li> </ul>	<ul style="list-style-type: none"> <li>Mechanical (i.e. physical CDs)</li> <li>Performance (radio, TV, concerts)</li> <li>Sync (movies, video games, ads)</li> <li>Digital/Other</li> </ul>

### Recorded Music Highlights



### Music Publishing Highlights



# WMG Challenges and Opportunities



## Treasury/Liquidity Characteristics

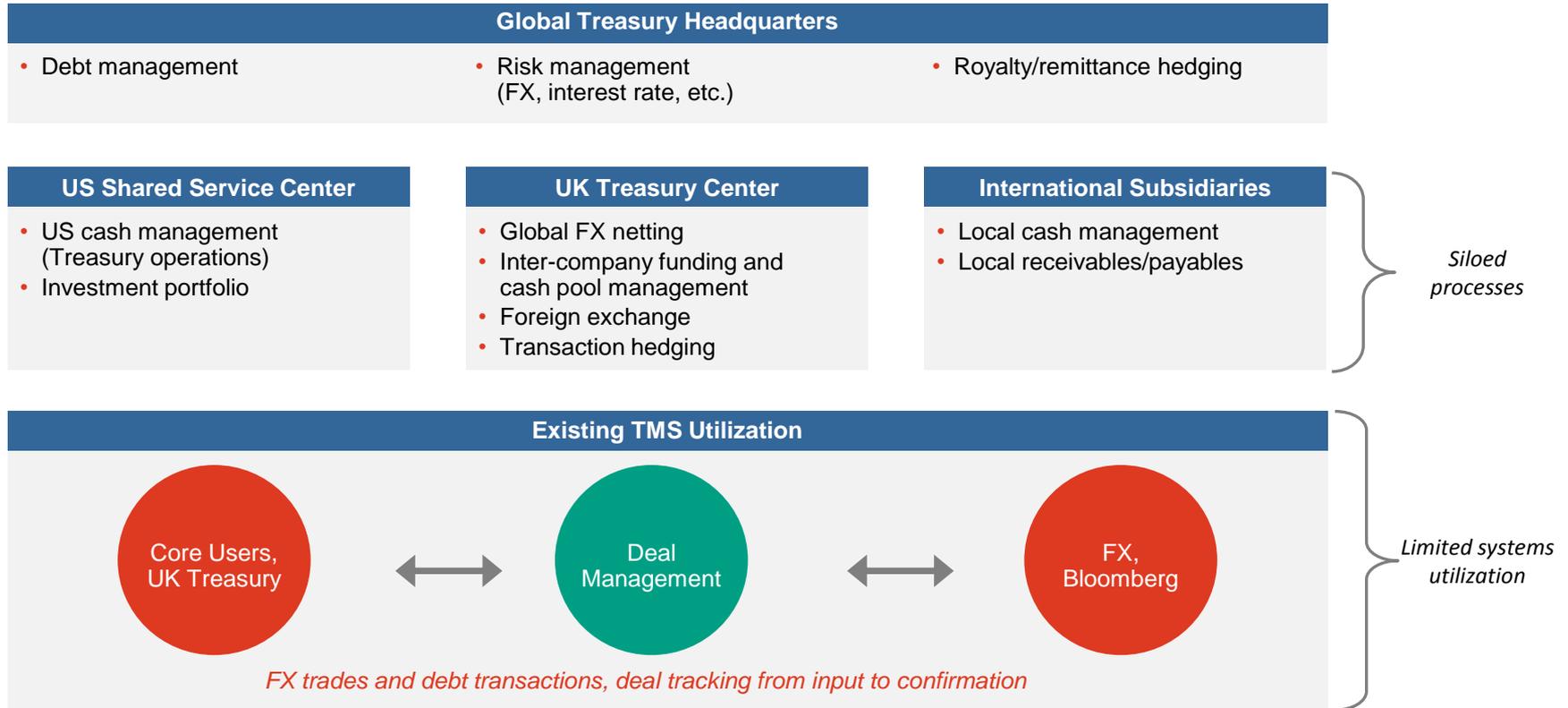
- **Decentralized Operations**
  - Operations in 50 countries, 75+ operating entities
  - Fiscal 2012 Revenues of \$2.8 billion, 40% from US
- **US Based Multinational**
  - \$2.9 billion total debt
    - Recent Acquisitions—£487 million EMI European Entities (Parlophone)
    - Recent Refinancings
  - US Artist and Repertoire (A&R)
  - US Headquarters
- **Repatriation and Liquidity Mechanisms**
  - Favorable US Tax Attributes
  - Intercompany Royalty/Distribution Agreements
  - Tax efficient repatriation
  - Inter-company Cash Management/ Loan Portfolio

## Legacy Treasury Organization

- **Control and Visibility of Cash**
  - 450+ Bank Accounts
    - Legacy System—weekly aggregation of Excel spreadsheets
    - Primarily concerned with GL accounts, not bank accounts
  - Treasury Management Systems
    - Upgrade to latest version of ASP service

# WMG Challenges and Opportunities, cont.

## Treasury Technology Landscape (2009)



# WMG Treasury Focus Areas



Treasury needs to constantly evolve to support and align itself with Global business.

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- Execute global bank balance reporting, bank rationalization strategies and increase technology use
- Create efficient liquidity structures and focus on cash/liquidity management
- Develop overall risk management framework and exposure management processes

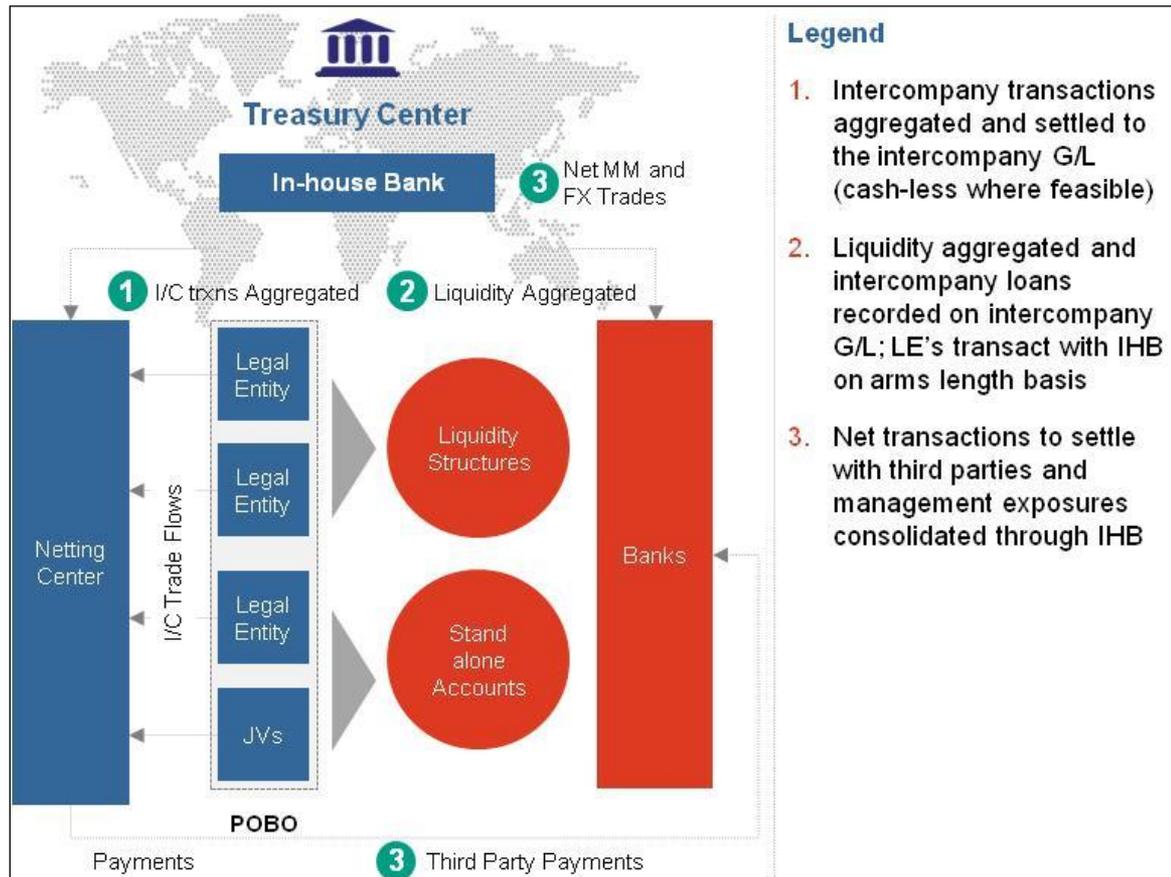
# Foundational Capabilities to Managing Global Liquidity



## Global Control and Visibility of Cash

- **Global Bank Inventory and Mapping**
- **Treasury Management Systems**  
(system upgrade to latest ASP version)
  - Treasury Optimization Plan—2009
  - Expand beyond deal management
  - SWIFT gateway capabilities, payment initiation and bank file import functionality
  - SWIFT connectivity for Bank Balance Reporting
  - Central tool for elimination of spreadsheets and double entry
- **Daily Global Cash Balance Reporting**
  - Real-time, centralized control and review of cash
  - Replaced legacy weekly excel file submission from affiliates
  - Banks mandates
  - Establishing and validating TMS bank accounts and mapping each to electronic reporting
- **Centralization of Treasury function to NY HQ**
  - Transition of treasury HQ operations; established NY Operational capabilities
  - Built out treasury team
  - Centralized bank relationships and FX trading to NY
- **Cash Forecasting**
  - Transitioned from quarterly, to monthly, to weekly methodology
  - Established global reporting methodology
  - Developed tool for daily liquidity evaluation

# In-House Bank Centralization of Liquidity & Risk



- Netting Center
- Intercompany Loan Portfolio
- Liquidity Concentration
- Next Generation:
  - Cashless Loans and Transactions
  - Third Party Pay-on-Behalf-of (POBO) and Receive-on-Behalf-of (ROBO)

Source: Citi

# In-House Bank Centralization of Liquidity & Risk, cont.



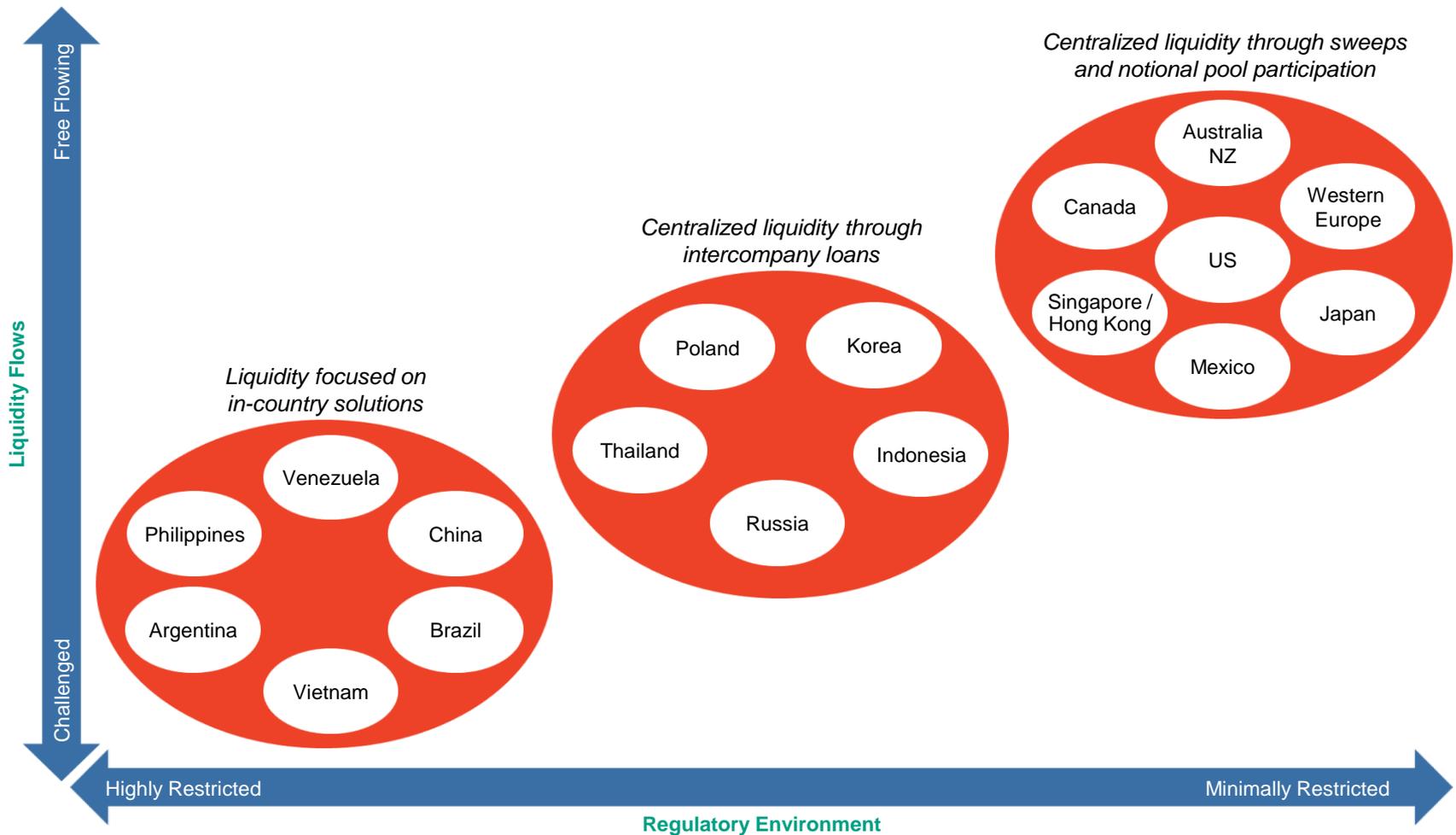
## In-House Bank Benefits

- Liquidity Management
- FX Management
- Subsidiary Funding and Repatriation

## Liquidity Management Constraints

- Regulatory Environment
- Tax Considerations
- Staffing/Technology/Accounting

# Liquidity Management Constraints: The Regulatory Environment



# Liquidity Management Constraints

- **Staffing, Technology, and Accounting**

- Restructured international treasury function

- Centralized function to NY, previously managed through WMI in London
- Automated Loan Register, eliminating manual spreadsheets

- Replaced outsourced treasury and accounting functions

- Leveraged technology to in-source Treasury execution and accounting reconciliation of loan transactions
- Developed new reporting and reconciliation capabilities through TMS
- Implemented automatic GL posting

- **Tax**

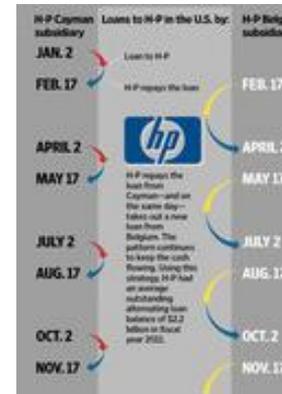
- US Tax Code - Section 956 Event-Deemed Dividend

- End of Quarter
- Withholding Tax Treaties
  - Australia, Canada
- Thin Capitalization

BUSINESS | March 28, 2013, 10:55 p.m. ET

## How Firms Tap Overseas Cash

*U.S. Companies Can Borrow Millions of 'Trapped' Funds From Foreign Units if They Follow the Rules*



Cash in Cash out—  
Consecutive Loans to use  
overseas cash without  
paying US taxes

*Wall Street Journal article, March 28, 2013*

# Pooling Structure Comparison



To address questions often raised regarding Notional and Physical pooling differences, the following table outlines the key considerations and differences between the two models.

	Multi-Entity Notional Pooling	Multi-Entity Physical Pooling (Sweeping)
<b>Description</b>	<ul style="list-style-type: none"> <li>• Single net group balance via full notional off-set across multiple currencies and jurisdictions</li> </ul>	<ul style="list-style-type: none"> <li>• Physical movement of funds between accounts, based on client-defined rules</li> </ul>
<b>Benefits</b>	<ul style="list-style-type: none"> <li>▲ Reduced reliance on bank funding without the need to commingle funds or alter currency exposure</li> <li>▲ Centralized control while maintaining subsidiary / operating unit autonomy</li> </ul>	<ul style="list-style-type: none"> <li>▲ Reduced reliance on bank funding</li> <li>▲ Facilitates same-day automated funding and concentration of cash on a domestic or cross border basis</li> </ul>
<b>Intercompany Loans Created</b>	<ul style="list-style-type: none"> <li>• Historically used to avoid intercompany loans, but subject to pool setup and interpretation</li> </ul>	<ul style="list-style-type: none"> <li>• Yes</li> </ul>
<b>Comingling of Funds</b>	<ul style="list-style-type: none"> <li>• No (see above)</li> </ul>	<ul style="list-style-type: none"> <li>• Yes</li> </ul>
<b>Withholding Tax Implications</b>	<ul style="list-style-type: none"> <li>• Historically used to avoid WHT on intercompany loans, but subject to pool setup and interpretation</li> </ul>	<ul style="list-style-type: none"> <li>• Intercompany position generated and subject to WHT if applicable</li> </ul>
<b>Participating Countries and Currencies</b>	<ul style="list-style-type: none"> <li>• Freely convertible and transferable currencies</li> <li>• Ability for bank to get right of setoff across participating countries</li> </ul>	<ul style="list-style-type: none"> <li>• Freely convertible and transferable currencies</li> </ul>
<b>Interest Calculation Support from Bank</b>	<ul style="list-style-type: none"> <li>• For Single-Currency Notional Pools, calculated on net notional balance of the pooling structure. For Multi-Currency Notional Pools, calculated at prevailing rate per currency minus a bank spread on total pool</li> <li>• Support for clients' arms-length compensation of pool participants – includes calculations and reallocation postings to support earnings and charges</li> </ul>	<ul style="list-style-type: none"> <li>• Calculated on consolidated position at the header account</li> <li>• Support for clients' arms-length compensation of pool participants – includes calculations and reallocation postings to support earnings and charges</li> </ul>

Note: Informational only – this cannot and may not be construed to imply tax advice. If advice is required, legal, tax or otherwise, you should consult your own advisors.

# Cash Mobilization

## Implementing Efficient Liquidity Structures



- **In-Country Pools**
  - Physical – Intercompany Loans
  - Notional – Interest Allocation
- **Cross Border Sweeping Structures**
  - End-of-Day physical sweeps creating Intercompany Loan Transactions
  - Automatic reconciliations and posting
- **Multi-Currency Notional Pools**
  - Intercompany Loans Aggregated at In-House Bank
- **Multi-Entity / Multi-Currency Notional Pools**
  - Entity Deposits Aggregated and Drained by In-House Bank

# Cash Mobilization

## Implementing Efficient Liquidity Structures, cont.

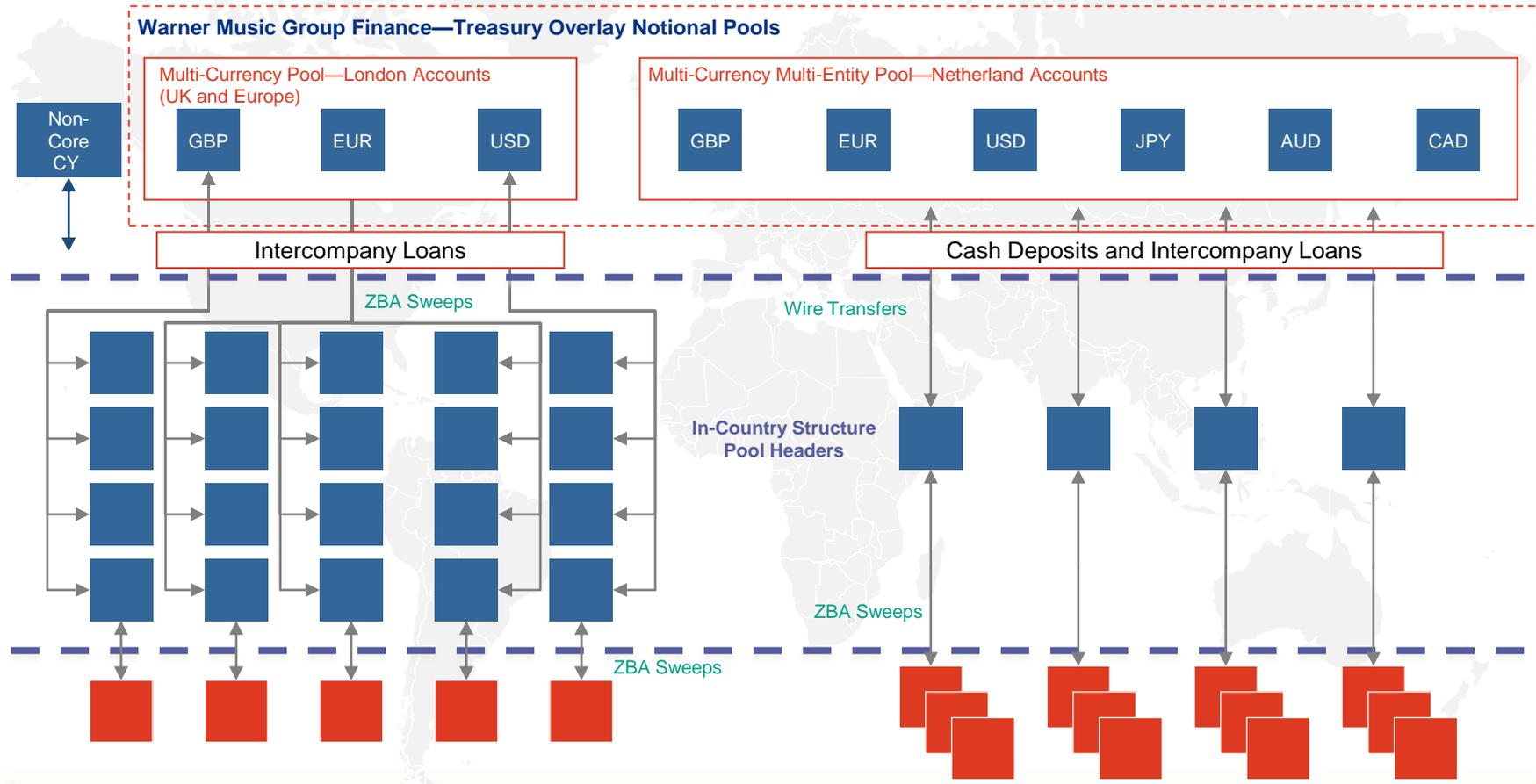


- **Cross Border Sweeping Structures**

- Optimal solution to manage subsidiary bank account balances
- Daily bank account balances sweep to zero End of Day
- Sweeps EURO, GBP to/from In-House Bank automates subsidiary funding process
- Automated subsidiary cash balance concentration
- Automated transaction reconciliation and GL posting
- Combined with Notional Pooling creates the optimal liquidity structure

# WMG Liquidity Structure

## US Concentration

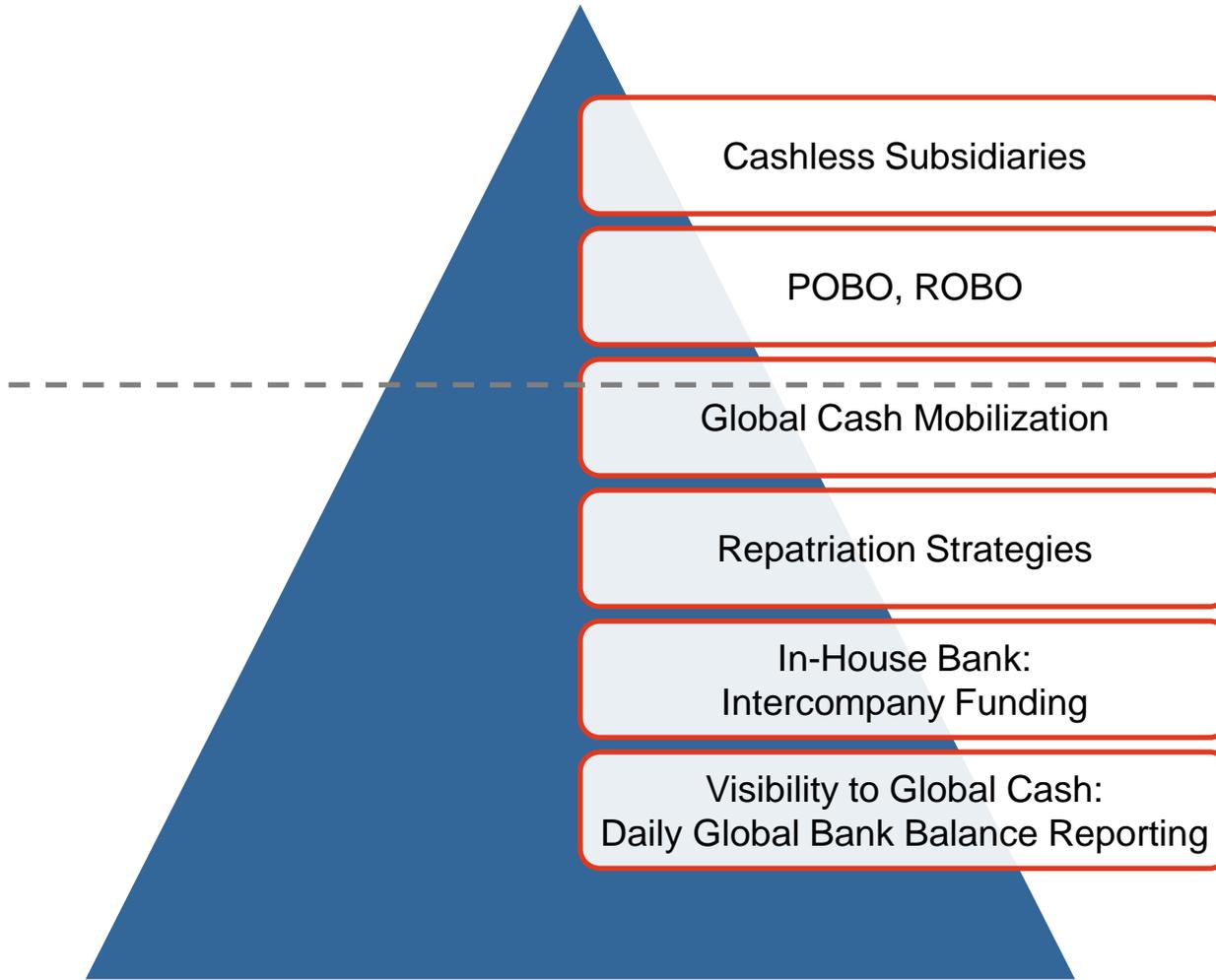


# Liquidity Structure Benefits

## Benefits

- ▲ Increased liquidity to reduce debt or increase investment
- ▲ Improve efficiency of both Treasury and subsidiary operations through automation
- ▲ Decrease bank fees through rationalization and scale
- ▲ Decrease sovereign risks

# Global Liquidity Pyramid



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