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At the 2002 TEXPO

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# **The Euro**

## **The Vision, The Reality, The Future**

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**TEXPO  
Dallas**

**April 8, 2002**



# Agenda



- ◆ **The Vision**
  - Key objectives and drivers
  - Euro timelines revisited
  - Key migration issues
- ◆ **The Reality - is the Euro a success?**
  - Macro overview
  - European payment system environment
  - Corporate treasury implications and trends
  - Opportunities to improve corporate treasury functions

# Agenda *cont'd*



- ◆ **The Future**
  - How will EMU evolve?
- ◆ **Conclusion**



# The Vision



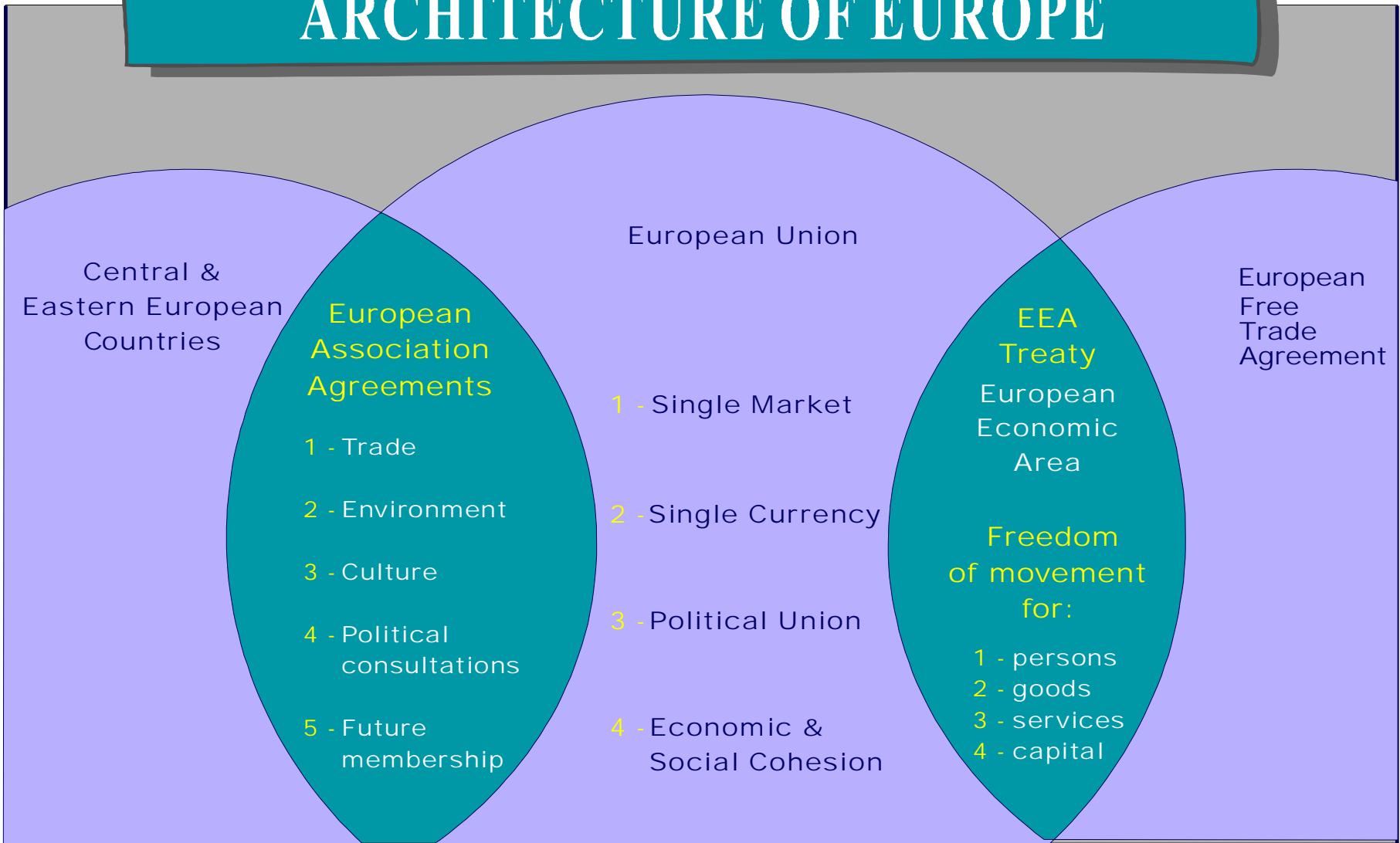
# European Monetary Union (EMU): Which Countries ?



- Austria
- Belgium
- Finland
- France
- Germany
- Greece
- Ireland
- Italy
- Luxembourg
- Netherlands
- Spain
- Portugal

# EMU is an integral part of a wider political vision of a united Europe

## ARCHITECTURE OF EUROPE



# Why Europe wanted a single currency: Advantages with EMU and the Euro

- ◆ **Stronger economic growth and employment**
- ◆ **More efficient (huge) single market**
- ◆ **Cuts costs**
- ◆ **International currency = increased stability**
- ◆ **Euro = international currency**
- ◆ **Prospects for more balanced international monetary relations**

# Revisiting the EMU Calendar

## Move to One Currency in Three Stages

“No compulsion, no prohibition”



2/3 May 1998

1 January 1999

1 January 2002

1 March 2002

Phase A

Transition Phase

Phase C

- Decided which countries join EMU
- Bi-lateral exchange rates pre-announced
- European Central Bank (ECB) established

- Euro-conversion rates fixed
- ECB took over monetary policy
- One euro money market rate



- Euro notes and coins
- Euro and national currency both legal tender
- All contracts and accounts automatically converted

- National currencies cease to be legal tender (timing varied by country)



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# Key Migration Issues



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# Key Migration Issues

- ◆ **Accounting and Reporting (internal and external)**
- ◆ **Contract conversions (derivatives, bonds, etc.)**
- ◆ **Bank accounts and information**
- ◆ **Treasury systems and procedures**
- ◆ **Pricing and invoicing (ERP systems changes?)**
- ◆ **Dual pricing (mainly at retail POS)**
- ◆ **...and CASH of course...!**

# Cash - the big challenge!

**5 billion coins and 15 billion notes - was it a big deal?!**

- **Logistical challenge**
  - **140,000 ATMs**
  - **4 mln POS terminals**
  - **7 mln vending machines needed recalibration**
- **Psychologically sensitive**
- **Massive information campaign**
- **Money laundering risk**
- **Counterfeiting**



# Costs

- ◆ **Total cost of changeover estimated by the ECB between 0.3%-0.8% of euro-area GDP (i.e. E20-50 bln)**
  - Probably on the low side and only accounting for direct costs
- ◆ **Costs borne by public sector and private sector roughly 50/50**
- ◆ **Costs are assumed where they arise - no government subsidies**
  - Thus the banking sector has absorbed a major portion of changeover costs

# The Reality



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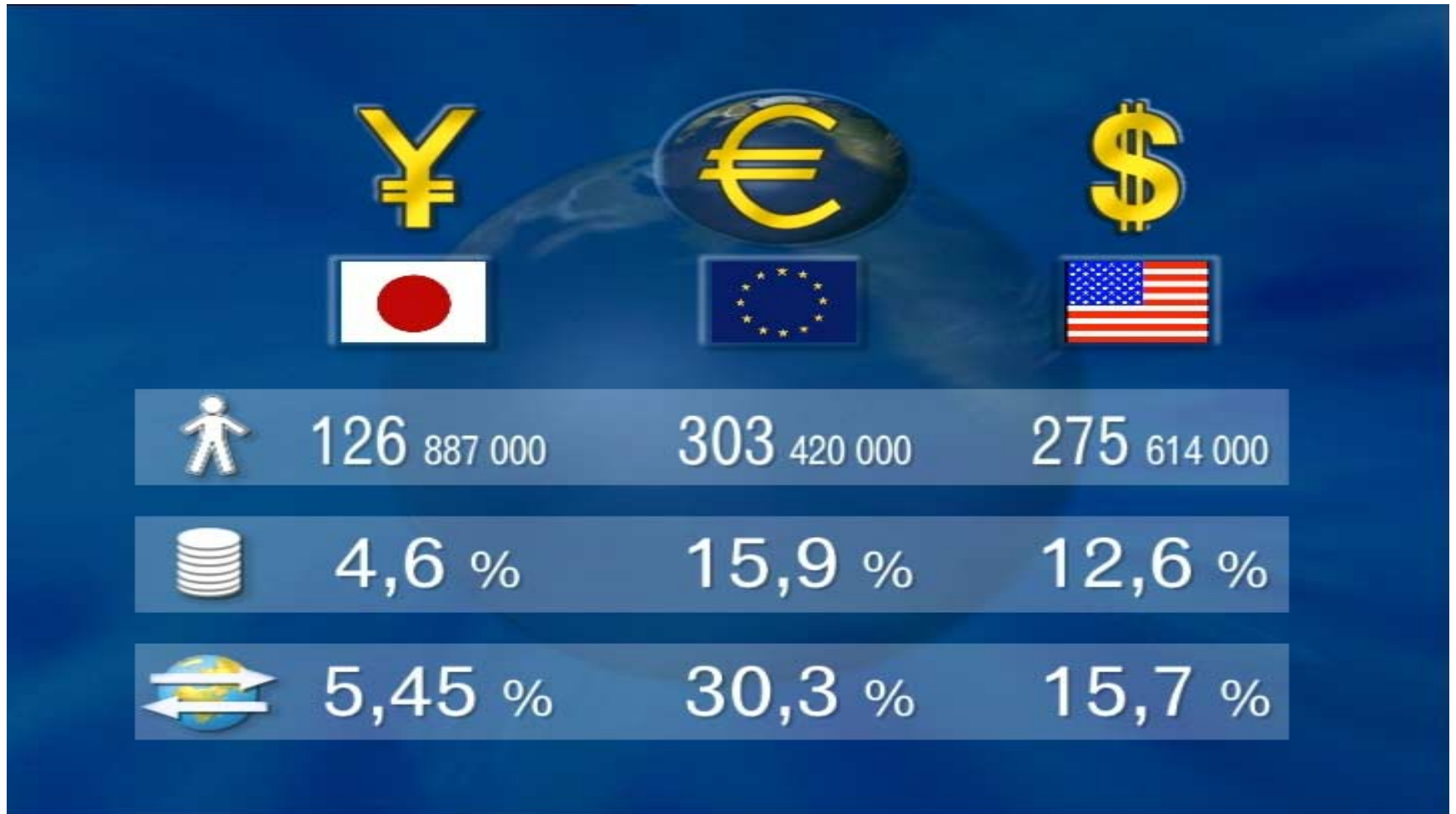
# Is the EMU really one market?

	USA	EMU
<b>ONE Currency</b>	✓	✓
<b>ONE Financial Market</b>	✓	✓
<b>ONE Jurisdiction</b>	✓	X
<b>ONE Payments Infrastructure</b>	✓	X

# Market Environment

- ◆ **Price transparency with EUR increases competitive pressure**
- ◆ **Harmonization (but slow on taxes)**
- ◆ **Growth of cross-border transactions**
- ◆ **Cost pressure and consolidation in payments industry**
- ◆ **Ongoing centralization of corporate treasury & cash management activities**
- ◆ **Pressure from Regulators to make the euro market efficient**
  - **EU Regulation on Cross-Border Transfers passed Dec 2001**

# Macro Overview



Source: The European Commission

# Debt Capital Markets

- ◆ **Record volumes and bigger deals in 2001**
- ◆ **Initially few issuers with jumbo deals, mainly auto and telecoms**
- ◆ **New issuers added to diversification**
- ◆ **Euro-denominated global debt totaled \$ 1.7 trln by end 2001**
- ◆ **US issuers accounted only for 168 bln**

Source: Thomson Financial Sec. Data

# Equity Capital Markets

- ◆ **Consolidation ongoing**
  - Euronext: marketplace incl. Paris, Amsterdam, Brussels, Lisbon and LIFFE
  - Still 10 separate national exchanges
- ◆ **Harmonization of regulations and legislation**
  - The EC is aiming for a “single prospectus”

## Stock Exchanges 2001

	Volume (\$ trlns)	No of Listings
London Stock Exchange	4.7	2,262
Euronext	3.2	1,539
Deutsche Borse	1.5	984
Nasdaq	10.9	4,152
NYSE	10.4	2,797

Source: The Exchanges

# The European Payment System Environment



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# Forces changing the clearing infrastructure in Europe

- ◆ **The “Regulators” - The EU Commission**
- ◆ **The Heathrow Group**
- ◆ **European Committee for Banking Standards**
  - The IBAN mandated 2001
- ◆ **SWIFT developments**

# Europe Payment Infrastructure and Standards

- ◆ **High value domestic and cross border routes**
  - **TARGET (European Central Bank (ECB) , Real Time Gross Settlement (RTGS) and local RTGS systems linked to TARGET (e.g. ELS-Germany, TOP-Netherlands, TBF-France)**
  - **Local non-RTGS (end of day settlement) (e.g. EAF-Germany, SNP-France)**
  - **EBA/EURO1 non-RTGS (end of day settlement)**
  - **Correspondent banks**
  - **Network banks with in-country clearing links**

# Europe Payment Infrastructure and Standards

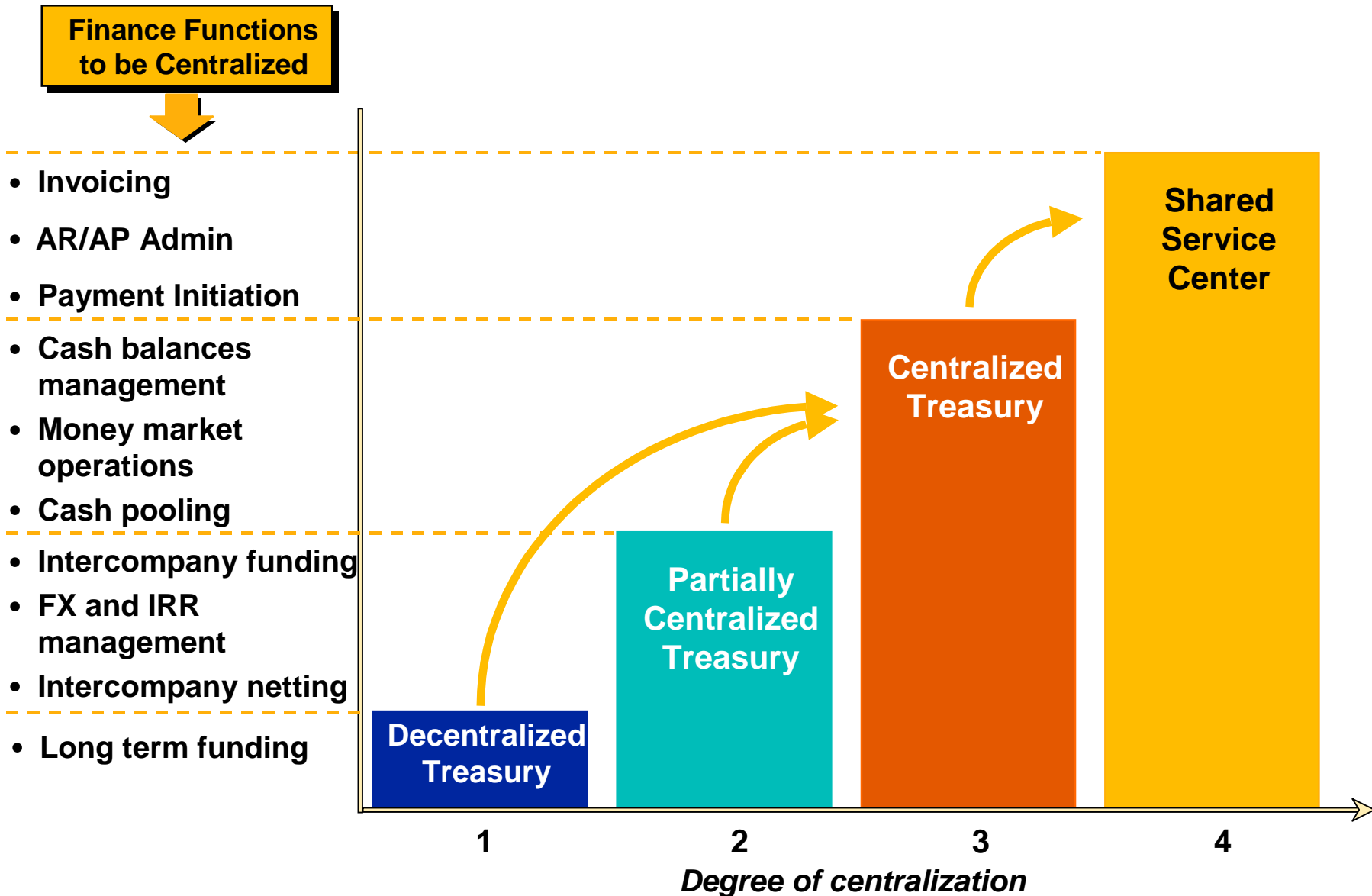
- ◆ **Low value domestic electronic payments (ACH)**
  - Generally efficient but no common system or format in place - tentative plans via STEP 1/2 for pan European ACH but no clear timetable. WATCH initiative is collapsing.
  - No link between the countries
- ◆ **Paper based payments**
  - No Europe wide system planned.
  - Volumes generally low compared with US and declining. Certain countries still use cheques relatively extensively - UK, France, Spain

# Europe Payment Infrastructure and Standards - New Developments

- ◆ **NewCHAPS**
- ◆ **RTGSplus (Germany)**
- ◆ **STEP1 (EBA low value cross-border)**
- ◆ **CLS/CLSB**
- ◆ **WATCH (global ACH) - in decline**
- ◆ **SWIFT (New releases e.g. MT103/MT102-3+)**
- ◆ **IBAN (ECBS)**
- ◆ **Trading, clearing and settlement systems**
  - consolidation of trading platforms

# The Reality - Treasury Implications and Trends

# Levels for Centralizing Treasury and Cash Management Services



# Euro - the Catalyst for Centralization

<b>Centralizing</b>	
<b>Transaction Processing</b>	<b>Liquidity Management</b>
<ul style="list-style-type: none"><li>• Improving efficiency by linking general ledger and bank infrastructure</li><li>• Business process re-engineering</li><li>• Local entities focus on core business growth</li><li>• Overall cost reductions</li></ul>	<ul style="list-style-type: none"><li>• Better insight into treasury positions</li><li>• Improved use of corporate cash</li><li>• Improved forecasting</li><li>• Interest optimization</li><li>• Rationalize banking relationships</li></ul>

*Technology - the enabler*

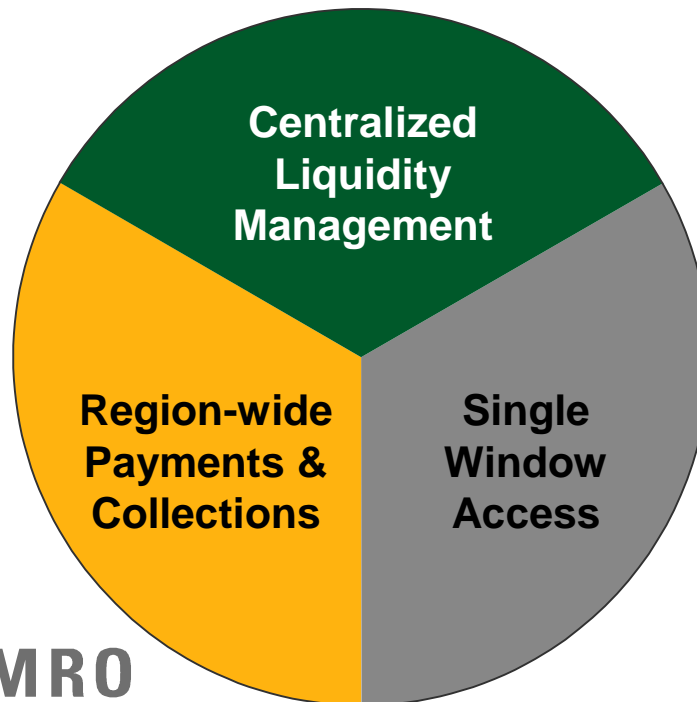


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# Benefits of a Full Regional Eurozone Bank Structure

- Centralized MM funding/investments
- Improved balance sheet
- Better forecasting
- Improved working capital management

- Minimized transaction costs
- Clarity on bank fees
- Reduced volume of cross-border flows
- Transaction execution at the right time
- Straight through processing



- Single electronic banking platform
- Consistent service levels
- Smooth account opening and implementation

# Opportunities to Improve Treasury Functions

# Opportunities to Improve Treasury

## Strategic:

- ◆ **Create single region (global?) business model**
- ◆ **Centralize cash management and create working capital saving opportunities**
- ◆ **Obtain real time financial overview of European business (Treasury integration & e-Treasury)**
- ◆ **Use depth and breadth of EUR debt capital market for investment and funding**
- ◆ **Risk management / hedging**
  - refocus from fx to interest rate hedging

# Opportunities to Improve Treasury

## Tactical:

- ◆ **Consolidate banking partners to:**
  - rationalize bank accounts
  - cut costs and leverage bargaining power
  - streamline service levels
- ◆ **Review critical mass for:**
  - consolidating treasury/EB infrastructure
  - establishing Shared Service Centre
    - ...or, consider outsourcing

***Early starters have paved the way and best practices have been established. Most companies are still running its treasury functions very decentralized however.***

# The Potential

**Best practice companies integrate the Euro transition with other re-engineering efforts to:**

- ***Realize maximum efficiencies***
- ***Gain competitive advantage***

# Summary of Key Trends in Europe

- ◆ Companies not realizing the full benefits of the euro
- ◆ Tax and regulatory issues require more attention than expected
- ◆ Most structures are still liquidity driven
- ◆ Companies focusing on streamlining transactions
  - First step - transfer local transactions to a regional European bank
  - Second step - centralize transaction processing within the company
- ◆ Companies expand cash management structures into central and eastern Europe

# Market Trends - Central & Eastern Europe

- ◆ **Countries deregulating to align with EU membership criteria**
- ◆ **Advantages of integrating CEE in West-European solutions still limited due to restrictions**
- ◆ **Corporates moving towards regional treasury management**
  - **Regional solutions can provide competitive edge**
  - **Benefits from standardisation across countries (pricing, services, transaction initiation)**
  - **Cross-border pooling remains difficult due to restrictions**

# The Future



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# Europe in the 21st century



- **Negotiations with 13 applicant countries has begun**
- **Expansion will support free trade**
- **Door remains open: any European country can apply to become a member of the Union**



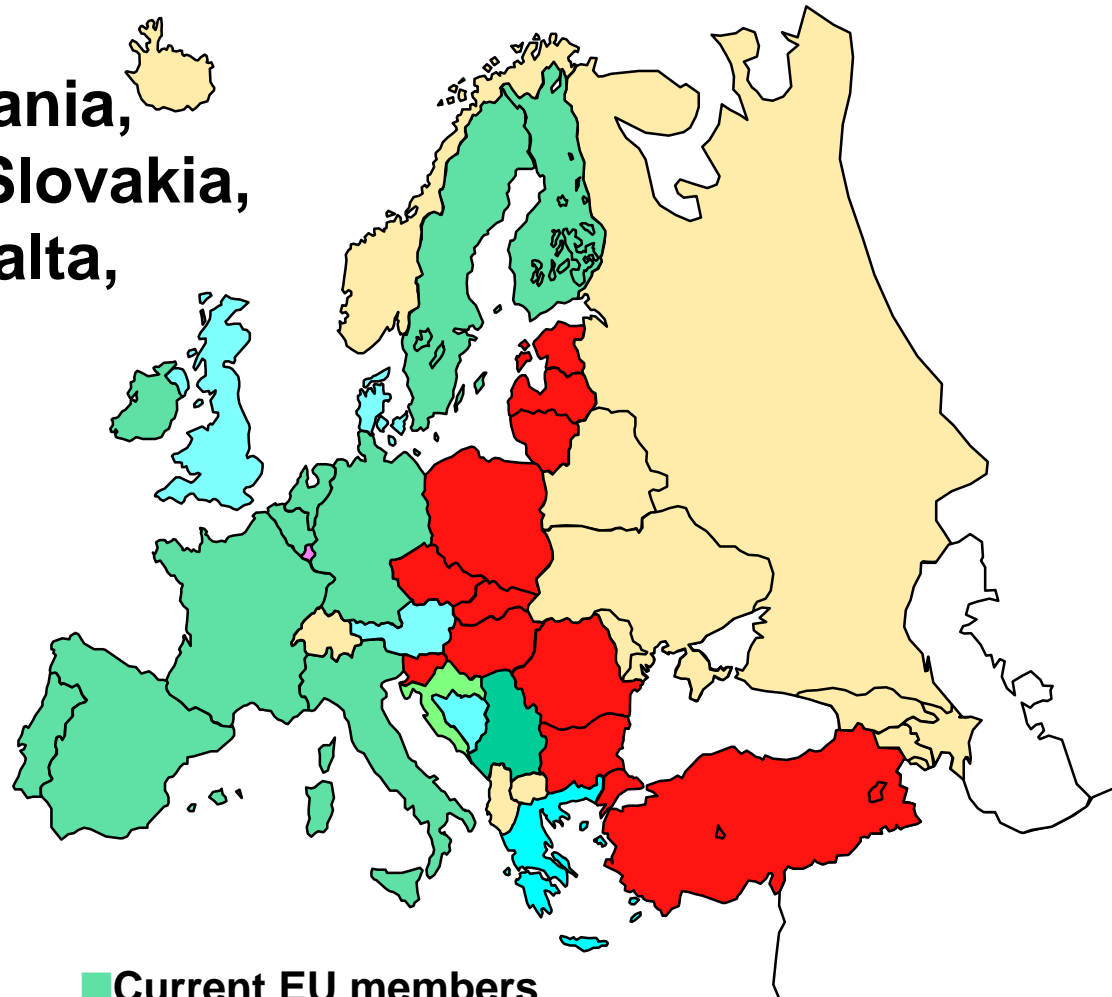
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# Applicant Countries

**Estonia, Latvia, Lithuania,  
Poland, Czech Rep., Slovakia,  
Hungary, Slovenia, Malta,  
Cyprus**

**Bulgaria, Romania**

**Turkey**



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■ Current EU members  
■ Applicant countries

# New EMU Members

- **Joining EU does not mean joining the euro!**
- **Adoption of common currency in stages must meet:**
  - **Overall economic criteria of EU (current, pre-accession stage)**
  - **EMU convergence criteria including ERM II participation after accession**
- **First wave of accessions prepared for 2004**
- **Not pre-determined which countries but may be 6 and up to 10**
- **Bulgaria and Romania target later date (2007)**
- **Turkey currently far behind**

# Conclusion: The Euro = opportunities for treasury operations

- ◆ **Increased centralization of local cash and liquidity management as tools continue to improve**
  - treasury management systems, bank services, straight-through processing via the web, etc.
- ◆ **Global liquidity management**
- ◆ **Transformation of commercial flows**
- ◆ **Further rationalization of bank relationships**

**Treasury's role continues to evolve from transaction processing to strategic center of excellence.**

**Questions?**



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