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What makes for a good borrower/lender relationship?

The panellists provided delegates with an insight into the senior treasurer perspective on the borrower/lender relationship.

The panel was chaired by **John Jackson**, Group Treasurer – **Severn Trent**, who was joined by **Daniel Maraggelis**, Deputy Treasurer – **Royal Mail Group**; **Bente Salt**, Head of Treasury – **Rentokil Initial**; **Neil Wadey**, Group Treasurer – **British American Tobacco**; and **Linda Williams**, Group Treasurer – **RPC Group.**

Advantages of bank lending

The panel discussed the advantages of bank lending in comparison to other forms of financing. Bank lending was felt to provide flexibility (particularly in relation to drawdown), confidentiality and contingent funding. Speed of funding was also a key advantage as banks are able to assess risk in a shorter period of time in comparison to the capital markets. Bank lending (in particular revolving credit facilities and acquisition term facilities) is a key source of finance for borrowers alongside access to the capital markets which is used for longer-term funding.

How banks are selected

Bank selection can sometimes be on a legacy basis depending on who is providing existing facilities. In an ideal situation, it would be good to have a couple of banks in each market where the borrower is doing business in order to both create competition and hedge against a bank exiting a particular market.

When looking at the make-up of their relationship banks, borrowers will look at the geographic footprint of the bank (to ensure the borrower's markets are covered), their specialisation, and their regulatory environment. Having a diversity of regulatory environments is key in order to offset any regulatory movements and dynamics. Lenders also need to have a competitive product, have a good rating and a good capital base.

Borrowers will tend to have a core set of banks which will provide both balance sheet funding and ancillary business requirements. However, there can be cases where core banks are not able to provide the necessary ancillary business and so a situation arises where a bank which is not providing balance sheet funding is providing ancillary business. As a result, borrowers may need to take the time to keep their banking arrangements under review to see if their business areas are actually covered by their core relationship banks.

Borrowers are keen to see their relationship banks earning a return so that they are incentivised to provide business. This is because having to change banks can actually be a difficult process which draws management away from their day job.

Approaches to relationship banking and allocation of ancillary business

A large borrower can have more than 20 core relationship banks, and deal with more than 100 banks altogether. Getting all the ancillary business into those core banks can be very difficult.

Senior treasurers will have discussions with their banks as to what ancillary business the bank can do and what they value. The location of a bank can affect what business a bank values. A borrower may look to estimate the profit arising from their ancillary business and try and share that amongst its banks, but ultimately the banks need to be competitive. Feedback is very important in this process and transparency is key; senior treasurers will look to have open conversations with their lenders.

Given the number of banks often involved, borrowers may look to sit down with their banks at least once a year in order to assess their relationship. This gives a bank a clear view of the borrower's business and enables a two way conversation to take place. Otherwise there can be significant time pressure on a treasurer trying to liaise with multiple banks and multiple specialists within those banks. In terms of ancillary business, it is up to a bank to find what the opportunities are and match their product to those opportunities. The borrower will help direct them, but the bank needs to have a product to offer.

Impact of different regulatory regimes on approaches to lending and ancillary business

An uneven regulatory landscape results in banks having quite different approaches to lending and to ancillary business. Some banks, for example at times UK banks which may be under pressure from the UK Government to lend to UK businesses, are more prepared to provide balance sheet funding without demanding as much ancillary, compared to banks based in the US for example. As a result borrowers will look to ensure that their relationship banks are made up of banks who are subject to different regulatory environments as this provides a natural hedge against such pressures.

Sustainability of relationship banking

A question was put to the audience as to whether doing business through relationship lending was sustainable given the increasing regulatory cost of capital. 58% thought it was sustainable only in the shorter-term (less than five years), with 31% believing it to be sustainable in the longer-term (more than five years). The panel considered this result and thought that it was becoming harder to achieve win-win outcomes, however, there is a scale overlay to this. Where you have a domestic business with less to offer in terms of ancillary business, then cost of capital could cause a short-term issue. A flight to quality borrowers could be expected with ancillary business being a key driver.

Whilst the market was expected to evolve with there being more advisory services providing structuring advice, the panel liked the current model of relationship banking. In particular, multi-product banks are appreciated by borrowers as they can give a joined up answer across a series of problems whereas a specialist bank cannot offer this rich dialogue.

The panel considered whether there would be an increase in pricing given currently low prices. Whilst this a potential risk from a borrower perspective, fundamentally banks need to be competitive and realistic about their return expectations. Borrowers would continue to look for different avenues and products to best suit their requirements.

The future

The panel concluded with a question to the audience as to how optimistic they were feeling about the future of the European loan market. 42% of the audience felt fairly optimistic, with 28% slightly optimistic.