THE GLOBAL ECONOMY

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Lessons on Borrowing… $200 Million at a Time

There I was, saying it in all seriousness: “Hey, fella! Can you spare $200 million?” The reply was nonchalant: “Let’s see what we get.” A few hours later, back came $220 million in the electronic equivalent of cold hard cash. The next day, a similar discourse. “How about another $200 million?” “We’ll find out soon enough,” was the response. The result: $195 million to add to the $220 million.

The routine went on for weeks, barely deviating from the script. Back in the late 1990s, it was my job to borrow cash for a major manufacturing company. We needed the extra money to help keep the wheels turning—and frankly, robust markets made it pretty easy. But have you read the headlines lately? Or watched your favorite stocks tank? In this jumpy market, the world of borrowing—so critical to the lifeline of so many businesses—has reached a curious stage that no chief financial officer can ignore.

The biggest market changes, of course, started earlier this year, when after months of being as subdued as a ripple-free pond, stocks started heaving up and down (so much so that one investment fund shuttered in a trice). As newbie financial analysts quickly learn, the bond market, where interest rates get set, and the stock market are inextricably linked, putting pressure on borrowing. Meanwhile, the Federal Reserve is still unwinding some of its “extraordinary measures” aimed at helping the economy recover from the mess of 2008-2009. Bottom line: more stock market volatility and higher interest rates.

That extra cost of borrowing, of course, won’t catch CFOs with decades of experience by surprise. The same is not necessarily true for those people who came of age in the decade since the financial crisis. That’s because interest rates have been extraordinarily low for an unusually long period. “Where they’ll get hurt is when they

see interest-rate levels that they might think are expensive but actually aren't," says veteran financier Steve Blitz, chief US economist at financial company TS Lombard. So borrowing cash at 3 percent might seem steep based on recent history—but it's a bargain compared to years past.

There are other ways that the world of borrowing hasn't changed. Investors are people, and they like to go with what they know, which is, of course, something good CFOs intuitively understand. Back in the 1990s, after a week of requesting $200 million a day, my contact said: "Our investors are happy buying the securities, but they just wish you'd be more consistent in the market." He had a good point. If the company is a frequent and reliable borrower, the lender has a greater level of comfort. So regularly dipping into the borrowing market when you don't need to will make it easier when you absolutely must get the cash. "It's just like when an individual builds up a credit rating," says Ivo Pezzuto, professor at the International School of Management, Paris, France. It's also smart for CFOs on the brink of needing cash to have already set up lines of credit with the bank.

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But what has changed is the way companies borrow. In the past, the choice for the CFO was frequently between the banks or the capital markets, with the latter closed to all but the most credit-worthy public corporations. That is no longer the case, which means it is harder for bankers to earn a crust but easier for savvy finance chiefs to borrow. For instance, why even bother with the bank when you can go directly to a marketplace loan maker (aka peer-to-peer lenders) who could issue a loan more quickly and at a lower cost? Loans can also be sourced directly via the web from many small investors, due to changes in the securities laws. "A lot of technology makes a lot of things faster and cheaper," says Pezzuto.

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