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SPECIAL ISSUE TREASURY, PART 3



IAFEI Quarterly

Special Issue Treasury

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Dear Financial Executive,

You receive the **IAFEI Quarterly, Special Issue, Treasury.**

This is another issue of the electronic professional journal of IAFEI, the International Association of Financial Executives Institutes. This journal, other than the IAFEI Website, is the internal ongoing information tool of our association, destined to reach the desk of each financial executive, or reach him, her otherwise, at the discretion of the national IAFEI member institutes.

The corporate treasury function has been, and is being, directly and immediately impacted by the ongoing worldwide financial crisis with its many diverse facets.

This present **Special Issue Treasury** provides you with a number of case studies of successful specific core activities of corporate treasury operations. The case studies are from famous corporations from several countries. Some of these corporations are represented through membership in IAFEI member institutes.

All case studies are self explanatory and reflect the high state of professional art in corporate treasury functions in the business world.

All case studies have been presented at the ACT Annual Conference, May 10 – 11, 2011, in Liverpool, United Kingdom, organised by **ACT, the Association of Corporate Treasurers, United Kingdom**. To this association, several IAFEI member institutes maintain good relationships, and through these IAFEI has got access to these case studies.

IAFEI is thankful for having received permission from the Association of Corporate Treasurers as well as from all individual corporate presenters of case studies, to include these case studies in the original form in this

Special Issue Treasury.

Once again, I repeat our ongoing invitation to IAFEI member institutes, and to their members, to send us articles for inclusion in future IAFEI Quarterlies, and to also send to us your suggestions for improvements.

This **IAFEI Quarterly**, like its predecessors, offers a variety of subjects. Enjoy reading them.

With best personal regards



Helmut Schnabel



Funding through the loan and bond market – the corporate experience

Rando Bruns

Head of Treasury, Merck KGaA

10 May 2011, ACC Liverpool, UK



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Merck at a glance

Company overview

- Oldest pharma and chemicals company in the world – since 1668; no link to Merck & Co. in USA
- Diversification in pharma, life science, and chemicals to spread risk
- Focus on specialty & niche markets
- ~70% family ownership; ~30% public ownership by shares
- Consistently profitable
- Major acquisitions: Serono (CH) in 2007 (CHF 16.6 bn) and Millipore (US) in 2010 (USD 7.2 bn)

Pharmaceuticals (Sales 2010: EUR 6.2 bn)

Merck Serono

Leading market positions

- Multiple Sclerosis
- Fertility
- Cancer Treatment



Consumer Health Care



Chemicals (Sales 2010: EUR 3.1 bn)

Merck Millipore

Leading market positions

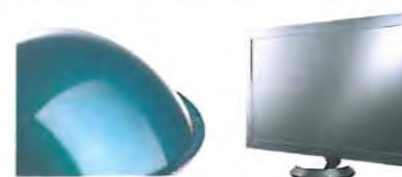
- Life Science tools



Performance Materials

Leading market positions

- Liquid Crystals
- Pearlescent Effect Pigments



Merck at a glance

Regional diversification

Sales by Region (FY 2010)

EURm



- Broad global presence with more than 40,000 employees
- Merck operates in 67 countries worldwide

Merck at a glance

Financial set up

- Important pillars of Merck's financial policy are:
 - Financial flexibility through diversification of funding sources
 - Syn loan is Merck's strategic reserve and defines the group of relationship banks
 - Solid investment grade rating at all times

Major Funding Sources	Frame	Utilization (31. March 11)	Comment
Cash / Marketable Securities	-	EUR 1,540m	-
Debt Issuance Program	EUR 10,000m	EUR 4,180m	Plus EUR 500m standalone
ECP-Program	EUR 2,000m	EUR 0m	not often used
Syndicated Revolving Loan Facility due 2014	EUR 2,000m	EUR 0m	pure back-up line

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The loan market

Preparation of acquisition financing Millipore

- In order to be prepared for a potential acquisition Merck met in 2009 with major relationship banks in order to get a feeling for their lending capacity, market expertise and personal expertise.
- Merck was invited to a selective auction process by Millipore Corp early 2010.
- Development of Merger Model together with M&A advisor
- Development of funding concept
 - Mixture of cash, loans and bonds
 - Search for group of arrangers

The loan market

Loan negotiations

- Draft Bridge Loan Agreement was developed by Merck
- The following banks were mandated:

Bank of America
Merrill Lynch



COMMERZBANK



- The same set-up of external counsels was chosen as during the last two major loan negotiations of Merck
- Merck communicated clearly some criteria as potential deal breaker with banks

The loan market

Major challenges during loan negotiations

- No benchmark transaction available
- Determination of Bridge Loan amount
- Risk aversion of banks, even for short time frames

The loan market **Syndication**

- Quick refinancing via the bond market was envisioned in order to use market opportunities and reduce fees
- Participation of banks in the bond issuance was linked to the participation in the syndication
- After the bond issues the bridge loan was reduced substantially and syndicated immediately thereafter
- Merck drove successfully the syndication process

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The bond market

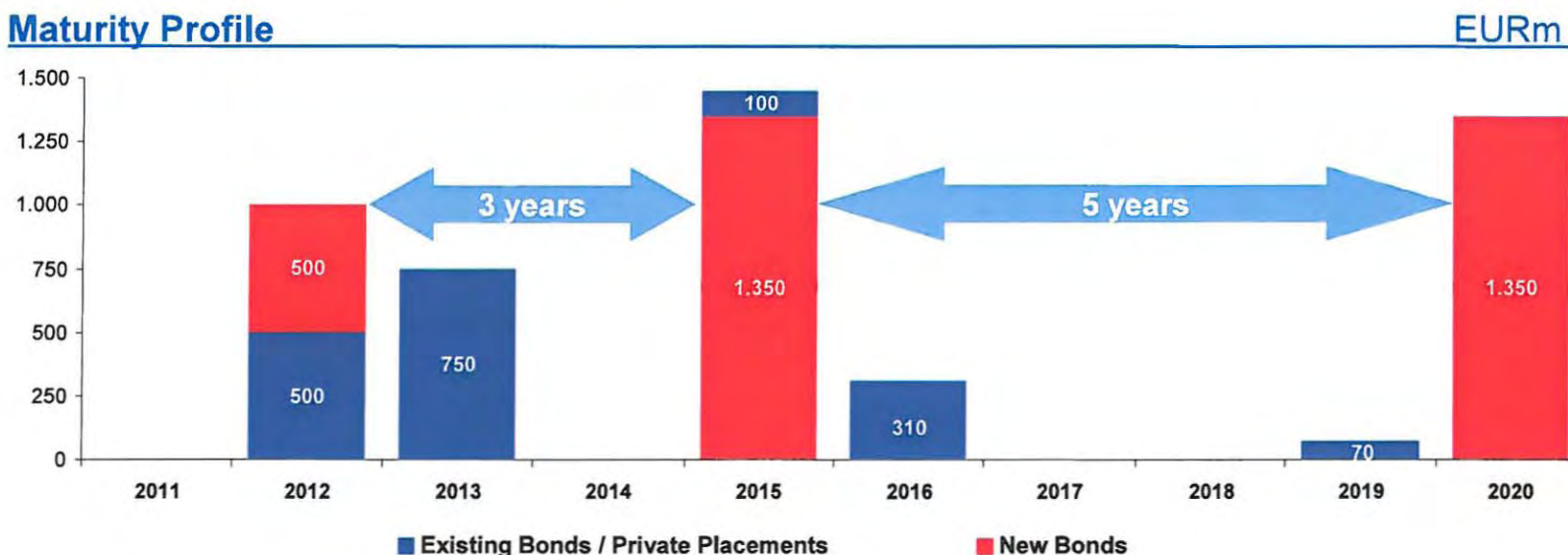
EUR 3.2 bn bond transaction

- Mandats to all participants in the SynLoan
 - BoAML, BNP and Commerzbank mandated as Active Bookrunners, all other syn loan banks mandated for a passive role
 - Equal treatment of all passive banks in terms of earnings and all banks in terms of league table credits
- No benchmark-transaction available
 - Market opener for deals of that size
 - Formulation of new M&A event call (101% if merger does not go through)
- Marketing and bookbuilding
 - Compressed calendar: only nine working days after signing on roadshow
 - Momentum built very quickly, books were closed within one hour
 - Bonds were seven times oversubscribed

The bond market Maturity profile

- Bond structure enabled investors to buy Merck yield curve:
 - Two year tranche: EURm 500; 75 bp over mid-swaps; Coupon 2.125%
 - Five year tranche: EURm 1,350; 100 bp over mid-swaps; Coupon 3.375%
 - Ten year tranche: EURm 1,350; 125 bp over mid-swaps; Coupon 4.500%
- Sound maturity profile for the entire Merck bond portfolio

Maturity Profile



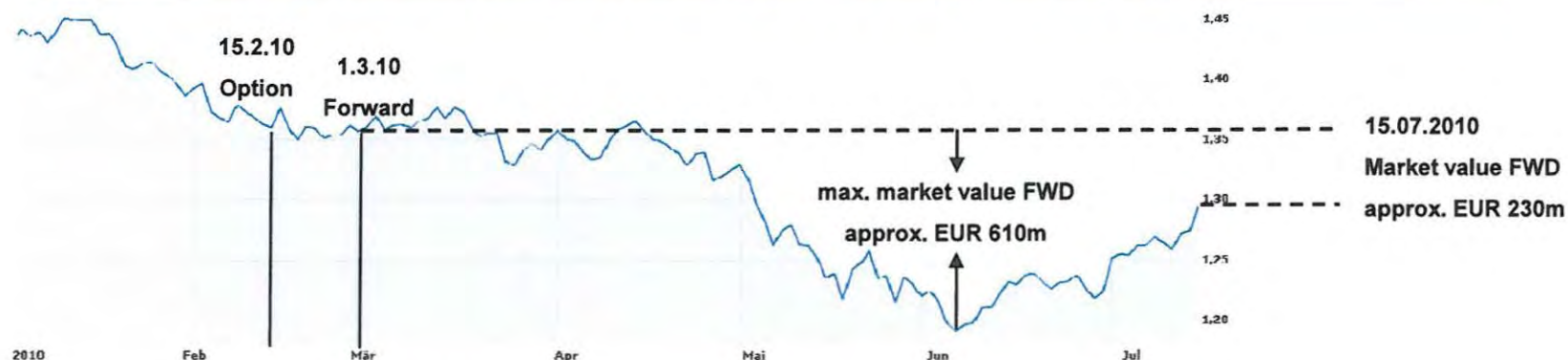
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FX management Purchase price hedging

- Due to the fx volatility and deal size hedging played an important role
 - Funding was executed in EUR, but purchase price had to be paid in USD
 - Option during auction process against „worst case“ of EUR/USD of 1.30
 - On the day of the acquisition agreement (Sunday) Merck started hedging via forwards at 1,35 with the opening of the Asian markets, finishing 20 hours later.

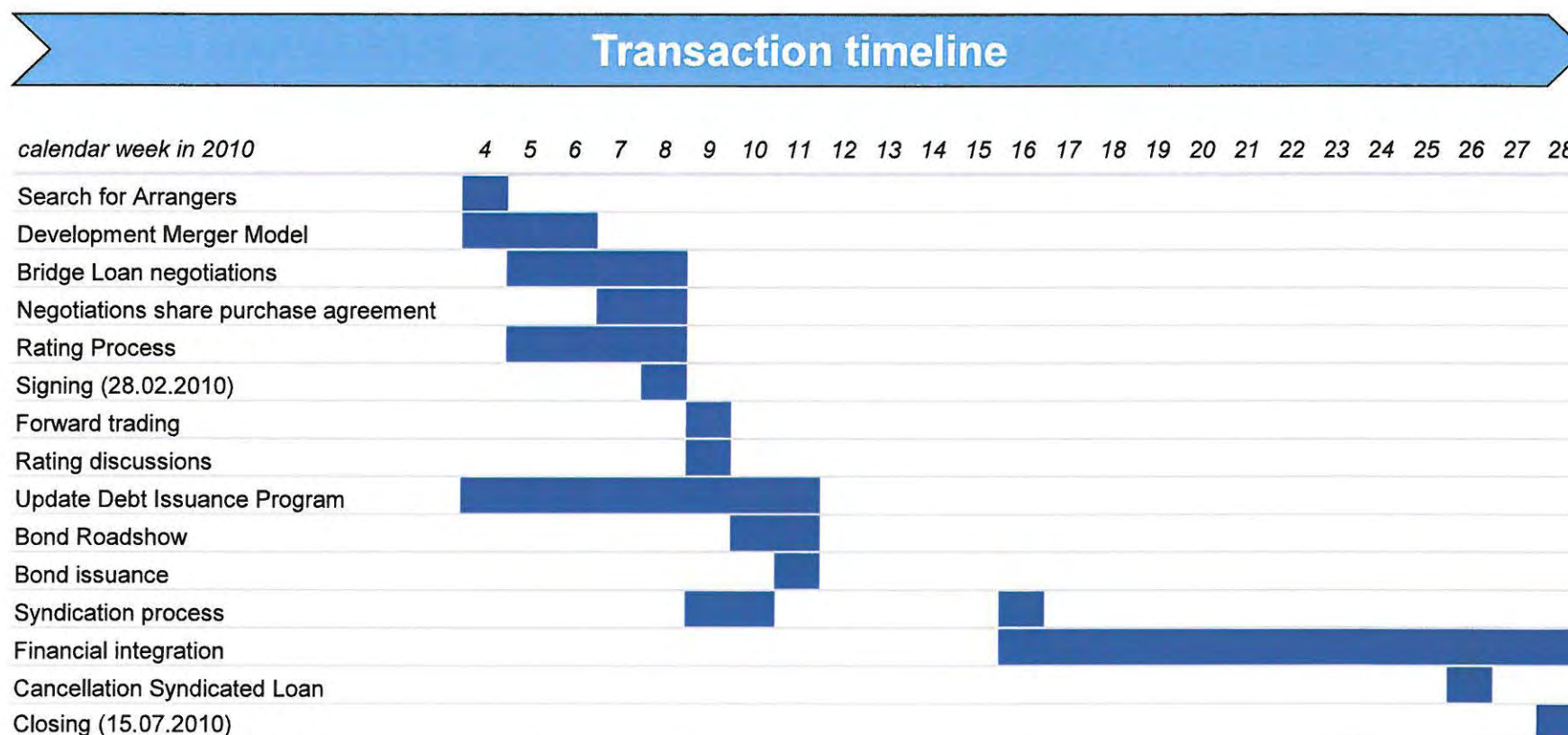
EUR/USD development between 01.01.2010 and Closing (15.07.2010)



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Timeline Important milestones



Result Successful transaction

- Bridge financing with attractive conditions was in place in time
- Appreciation of the transaction by rating agencies: BBB+/Baa2 rating outcome
- Successful and fast bond issuance at attractive pricing
- Successful syndication with further strengthening of Merck's relationship-approach

Treasurer:
Treasury of the year 2010



IFR:
EMEA Loan of the year



Euroweek:
**Corporate issuer with the best
M&A related bond funding**



ACT:
Bond Deal of the Year

Credit magazine:
**Euro investment grade
corporate deal of the year**



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Lessons learnt

- Prepare yourself well ahead of any potential transaction (DIP, CP, rating)!
- Competent lawyers on corporate as well as bank side facilitate effective negotiation!
- Use only one merger model and share it with relevant parties!
- Pace is key!
- Keep involved team as small as possible to ensure confidentiality!
- Avoid any discussions about league table credits – this can be painful!
- Keep your promises – you will benefit from that in the future!
- Ensure lawyers have a proper fax machine!

Thank you!

In case of questions please contact

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Economic Outlook and Corporate Ratings Review

Chris Dinwoodie
Managing Director, Head of Corporate Ratings
Standard & Poor's

ACT Annual Conference
10 May 2011

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Core Eurozone (and UK) Driving the Recovery

Main European Economic Indicators

	Germany	France	Italy	Spain	U.K.	Ireland	Eurozone
Real GDP (% change)							
2009	-4.7	-2.6	-5.1	-3.7	-5	-7.6	-4
2010e	3.6	1.6	1	-0.2	1.7	0.1	1.7
2011f	2.5	1.7	1.1	0.7	2.2	0.3	1.9
2012f	2.1	2	1.5	1.5	2.5	1.7	2
CPI inflation (%)							
2009	0.2	0.1	0.8	-0.2	2.2	-4.5	0.3
2010e	1.1	1.5	1.5	1.7	3.2	-1	1.5
2011f	1.5	1.6	1.8	1.8	3.3	0.3	1.8
2012f	2	1.8	2	1	2	0.5	1.8
Unemployment rate (%)							
2009	8.2	9.1	7.8	18	7.7	11.9	9.5
2010e	7.7	9.4	8.5	20.1	7.8	14.1	10.1
2011f	7	9	8.5	21	7.7	15	9.8
2012f	6.5	8.5	7.9	20.5	7.5	14	9.5

Source: Standard & Poor's 26 Jan 2011

e--Standard & Poor's estimate. f--Standard & Poor's forecast.

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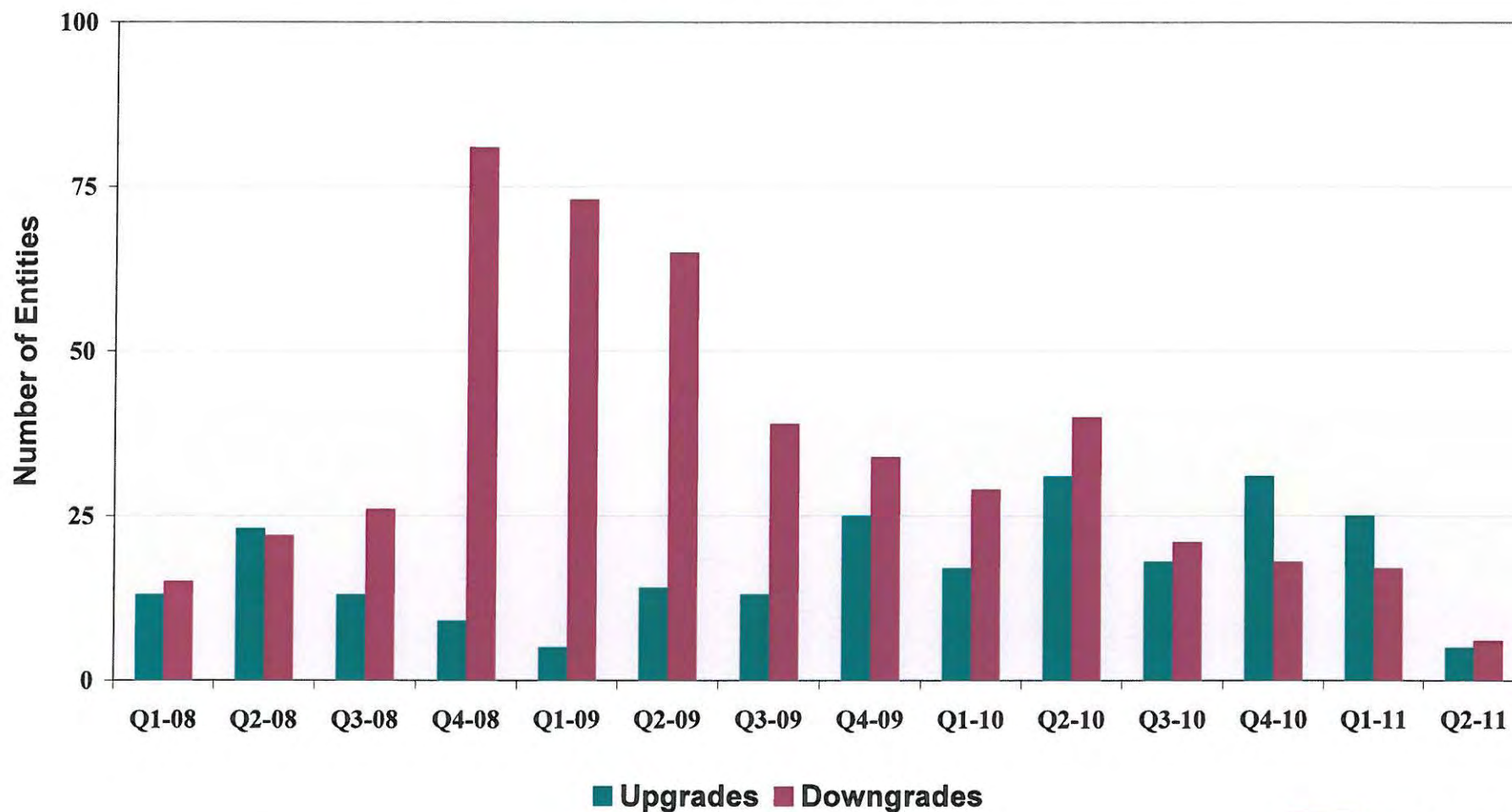
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Upgrades Predominate Q410-Q111

EMEA Industrials Quarterly Rating Changes by Number

(Source: S&P 15 Apr 2011)

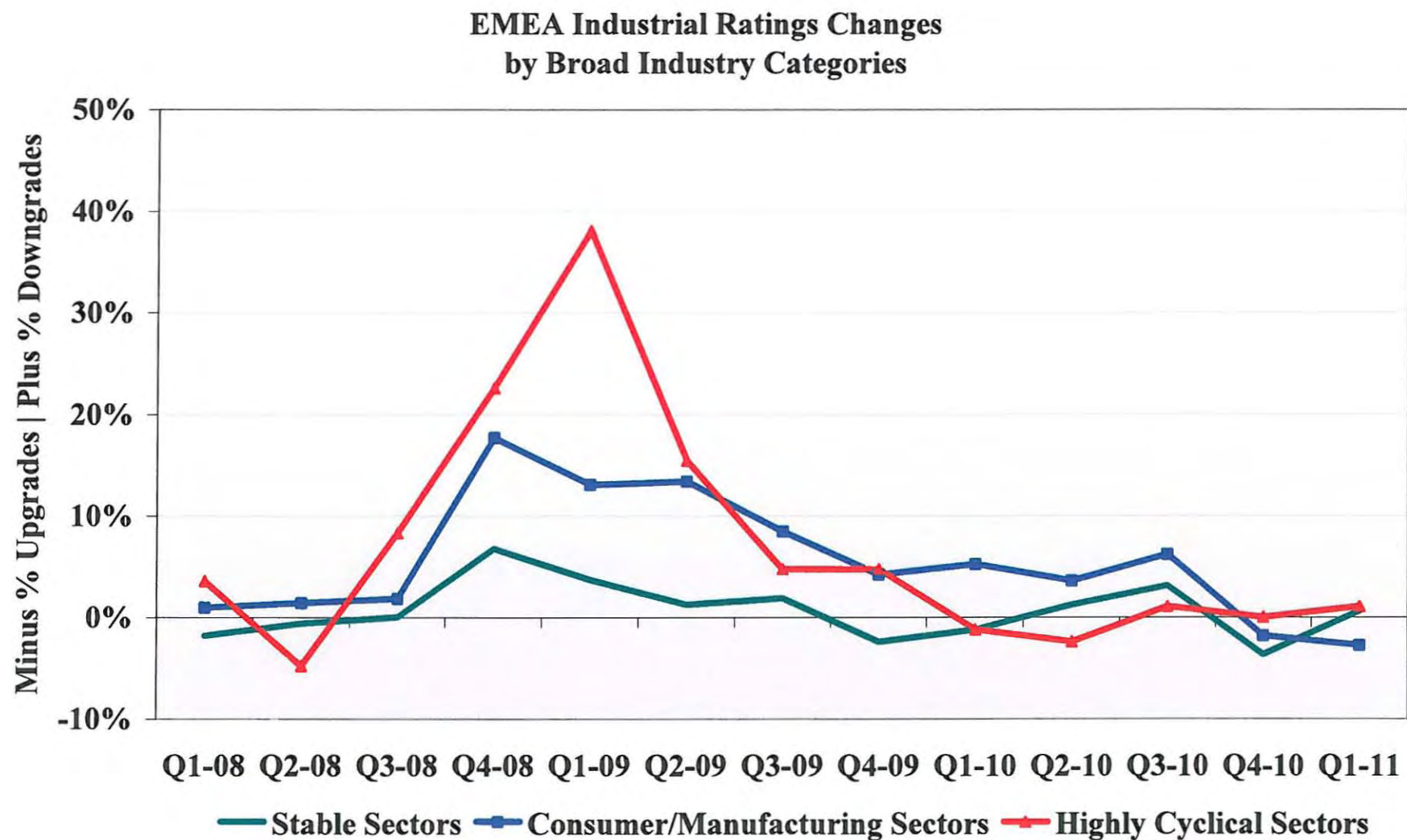


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Overall Ratings Stability Returns



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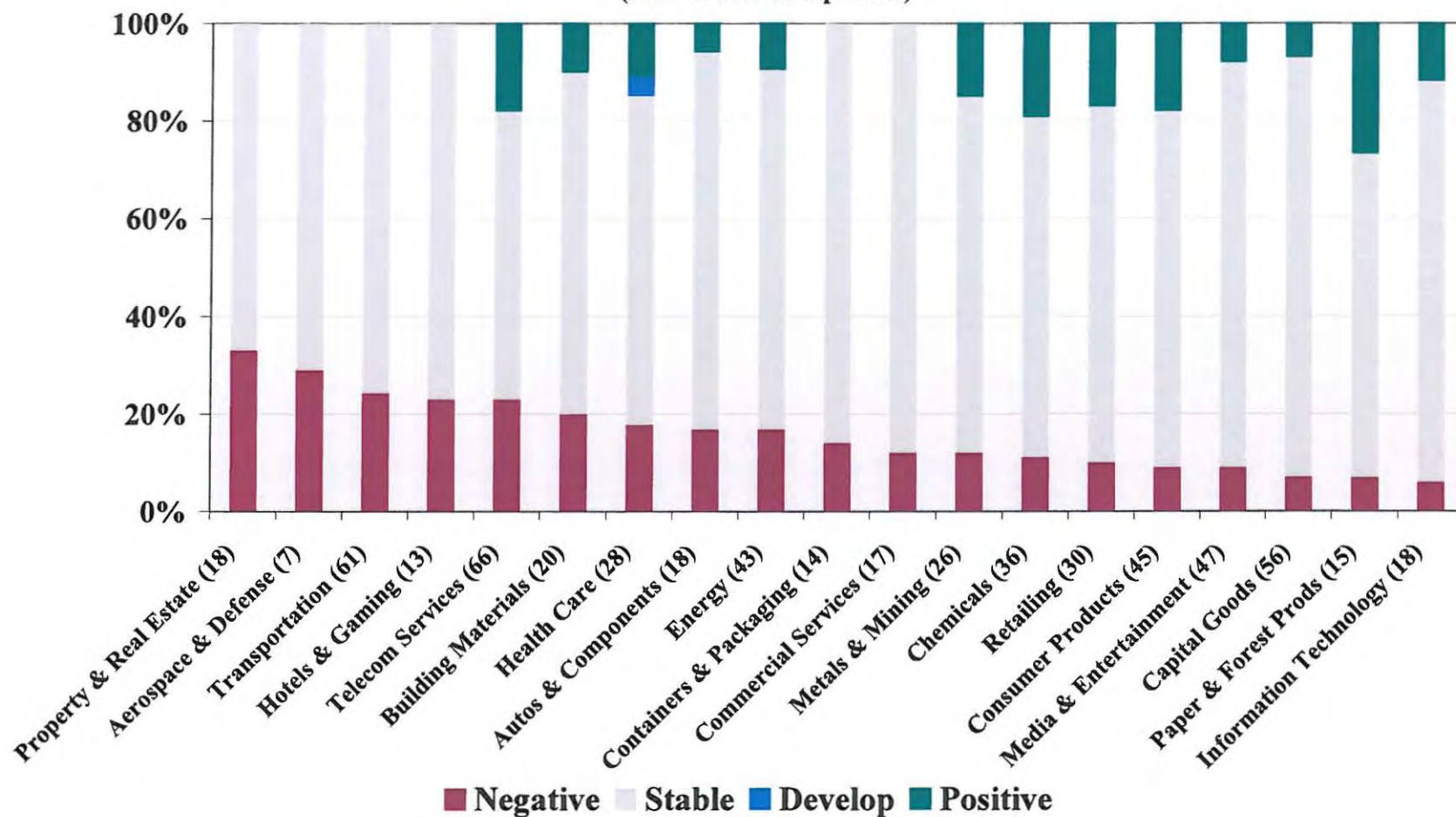
Source: S&P April 2011

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Normalisation in % Negative Outlooks Today

EMEA Industrials: Outlook/CreditWatch

(Source: S&P 15 Apr 2011)

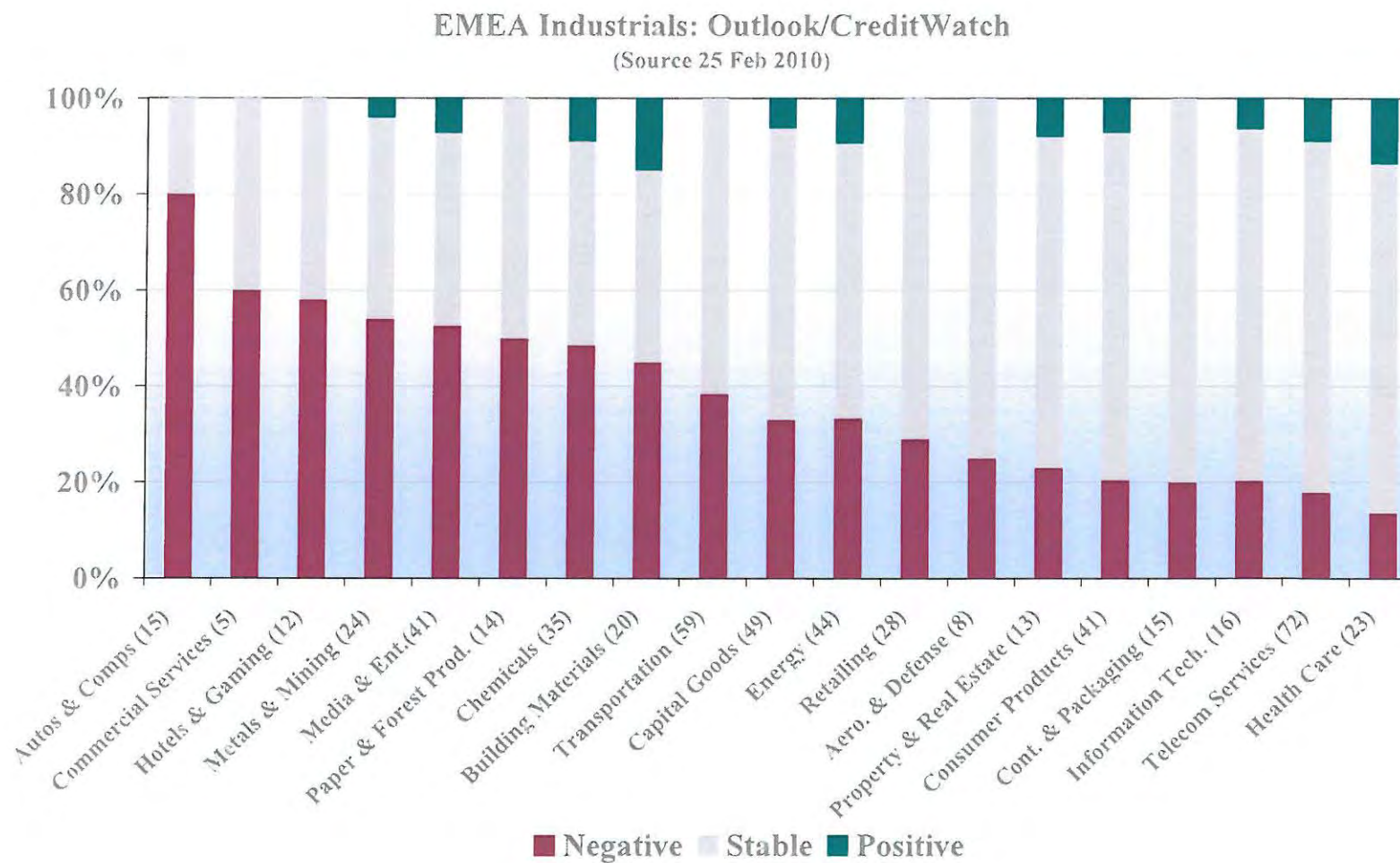


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...Much Higher Proportion With Negative Outlooks A Year Ago



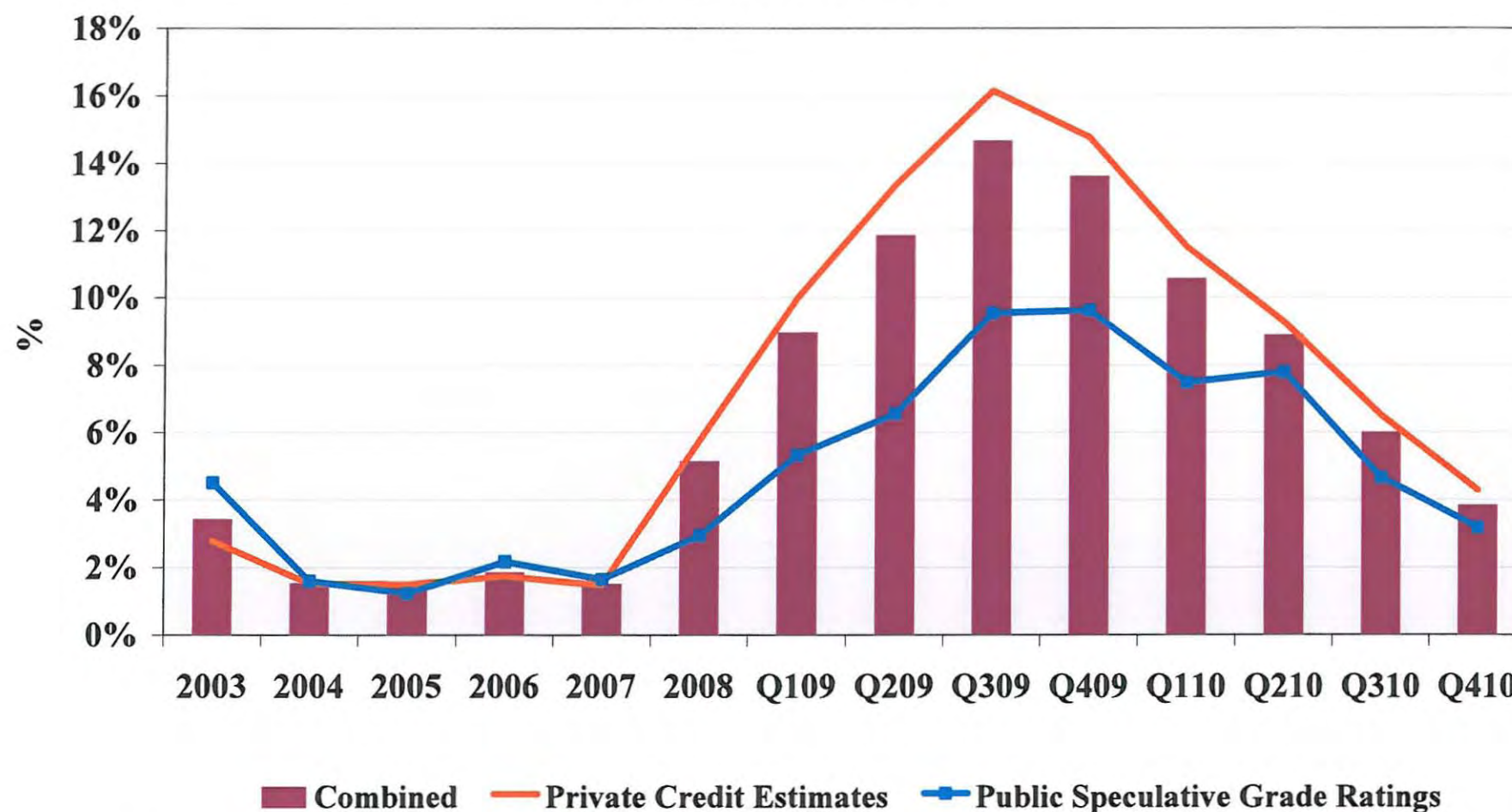
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European Speculative Default Rate Back Below LT Average

European Sub-Investment Grade Default Rate
(trailing 12mths %)



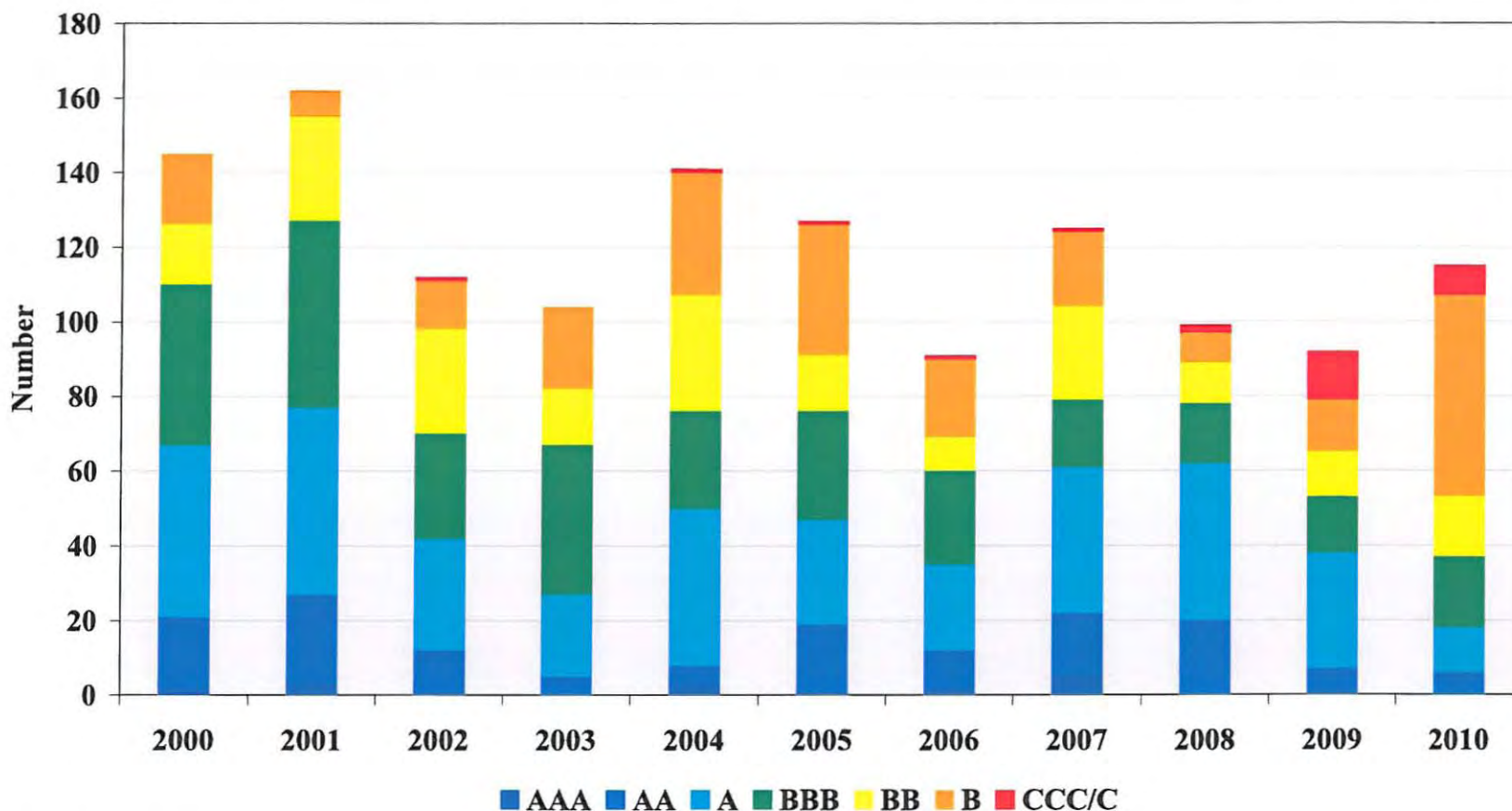
Source: S&P April 2011

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Significant Increase in Corporates Tapping High Yield Market

New European Corporate Ratings by Ratings by Category 2000-2010



Source: S&P GFIR and S&P CreditPro April 2011

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