

# Cash Management Tune-Up: Investment Products and Strategies

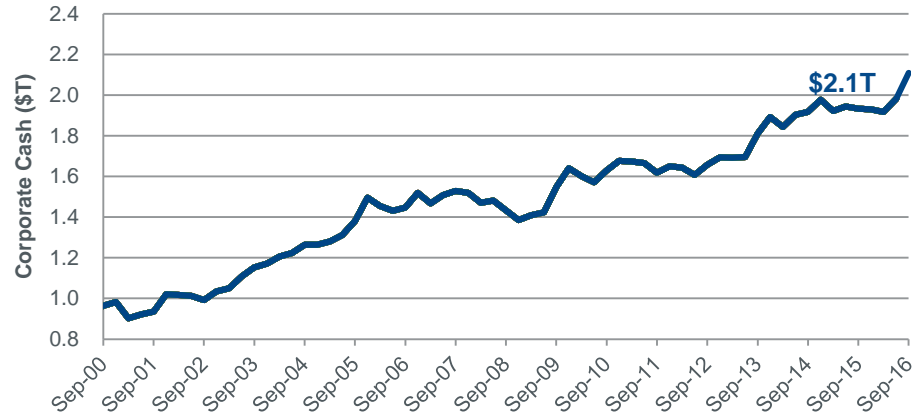
Ian Rasmussen, Investor Development, Fitch Ratings

April 2017



# Corporate Cash Levels – Higher Than Ever

US Corporate Cash



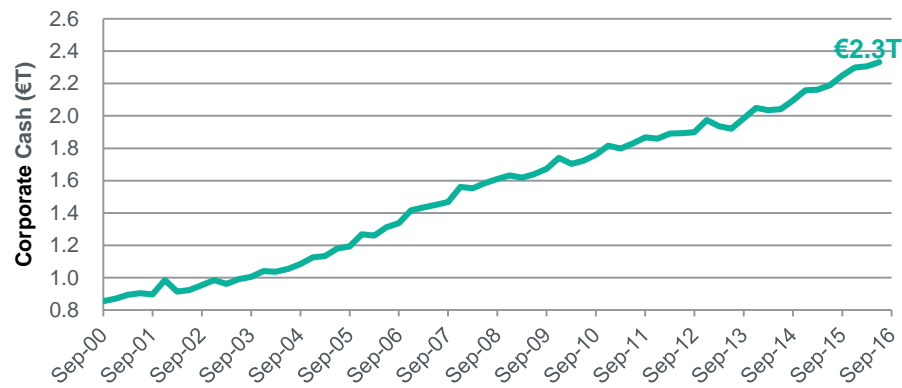
Source: Federal Reserve, Treasury Strategies

UK Corporate Cash



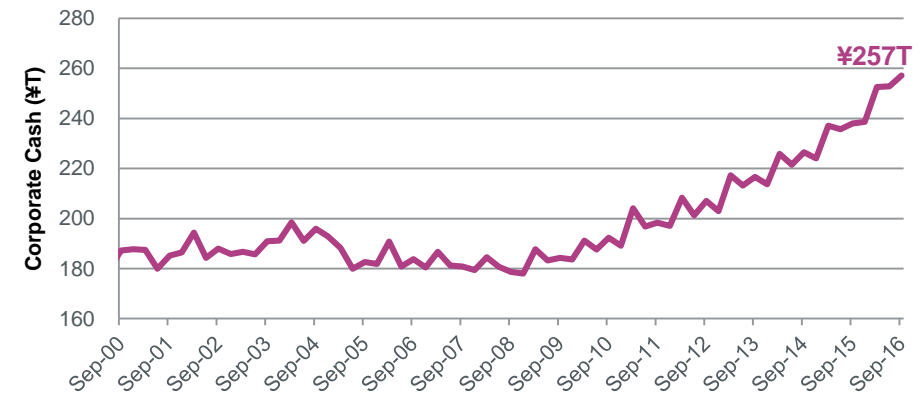
Source: UK Office for National Statistics, Treasury Strategies

Eurozone Corporate Cash



Source: European Central Bank, Treasury Strategies

Japan Corporate Cash



Source: Bank of Japan, Treasury Strategies

# A New Landscape for Cash Management

CHALLENGE	IMPACT
<p><b>BASEL III:</b> Regulations penalize banks for relying on less-stable wholesale short-term funding.</p>	<p>Banks to turn away certain corporate deposits. Reduced bank issuance of short-term debt, limiting the supply of high-quality, short-term investments.</p>
<p><b>ALTERNATIVE CASH MANAGEMENT PRODUCTS:</b> Money fund regulation is leading asset managers to develop 'alternative' cash management products such as private unregistered funds, short-term bond funds, separately managed accounts and 60-day maximum maturity money funds.</p>	<p>Treasurers and cash managers will need to evaluate the new products and update investment guidelines to incorporate these new strategies. Emerging products are not as tightly regulated as traditional money funds, allowing for greater flexibility, but also the potential for greater risk and less transparency.</p>
<p><b>CHANGING INTEREST RATE ENVIRONMENT:</b> Yields in the U.S. remain extremely low and have turned negative in Europe and Japan; however further divergence in monetary policy. Raising rate environment expected for the U.S.</p>	<p>Treasury professionals will need to re-think their cash management strategies and policies. Cash forecasting is valuable to better structure cash to meet changing market dynamics.</p>
<p><b>SUPPLY OF SAFE, LIQUID INVESTMENTS:</b> Supply of high-quality, short-term securities continues to shrink. Criteria also increasingly divergent – post money fund reform rating criteria as an example.</p>	<p>Flexible investment guidelines increasingly to ensure access to desired investments. For example, outdated investment guidelines that fail to include all of the 'big three' rating agencies (Fitch, S&amp;P and Moody's) unnecessarily decrease investment opportunities. Rating criteria for money funds not the same across all three agencies, creating new risks.</p>
<p><b>REGULATION UNCERTAINTY AND IMPLEMENTATION:</b> European Money Fund Reform, Cash repatriation in 2017? Reg 385 brings increased documentation and reporting.</p>	<p>Funding business operations, especially for global corporations more complex. Managing investment liquidity, documentation and reporting and structuring cash are strong focus for 2017.</p>

# Cash Management Options Increasing

PRODUCT	COMMENT	VALUATION	REDEMPTION RESTRICTIONS	REGULATED	RESTRICTED ACCESSIBILITY
Bank demand deposit	Bank – Basel III Constraints	Stable	No	Yes	No
Time/certificates of deposit	Bank – Basel III Constraints	Stable	Yes	Yes	No
Private money funds	Newer for treasurers, low utilization	Stable (generally)	By contract	No	Yes (large clients)
Ultra-short bond funds	More utilization	Floating NAV	Some	Yes	No
Short-duration ETFs	Low utilization by treasurers, differing investment standards	Floating NAV	No	Yes	No
Separately managed accounts	Traditional option, increased usage for corporates segmenting cash	Book/Market value	No, investor may bear gain or loss	No	No
Retail prime MMFs	MMF reg constraints, declines. Natural person = retail investor	Stable NAV	Yes, fees & gates	Yes	Yes (retail only)
Inst. prime MMFs	Most MMF reg constraints, declines	Floating NAV	Yes, fees & gates	Yes	No
“Short maturity” prime MMFs	Manager – prime fund designed to mitigate MMF reg concerns. Increasing utilization	Potentially stable	Yes, but potentially less likely	Yes	No
Government MMFs	Primary option as treasurers re-allocate cash	Stable NAV	No	Yes	No
Structured bank deposits	FDIC insured bank deposits above \$250,000	Stable NAV	Yes (T+1)	No	Yes (Max \$100mm per Tax ID)
Direct investments in money market instruments	Increasing importance in CP market, for investors that have measurable cash flows	Book/Market value	No, but investor bears losses on sale	No	Some

# Value Proposition of Money Market Instruments

Imagine the perfect liquidity management instrument. Let's call that 100 on a 0-100 scale:

- High relative yield
- Daily liquidity
- Ultra-low risk
- Low minimum transaction size
- Low fees
- Diversification
- Convenience
- TMS connectivity
- Portfolio accounting
- Professional management

# Instrument Attributes – Today

	Prime MMF	Treasury MMF	T-Bills/ Repo	Bank DDA	Ultra-Short Bond Funds	Direct CP	SMA's	In-House Mgt
High relative yield	x				x	x	x	x
Daily liquidity	?	x	x	x	x	x		
Ultra-low risk	x	x	x	x				
Low minimum transaction size	x	x		x	x			x
Low fees	x	x	x	x		x	x	x
Diversification	x	x			x		x	
Convenience	?	x		x				
TMS connectivity	x	x	x	x				
Portfolio accounting	x	x		x	x		x	
Professional management	x	x		x	x		x	

Source: Treasury Strategies

# Value Proposition of Money Market Instruments

Investor utility of each instrument before and after the post-crisis regulations (Dodd-Frank, Basel III, MMF):

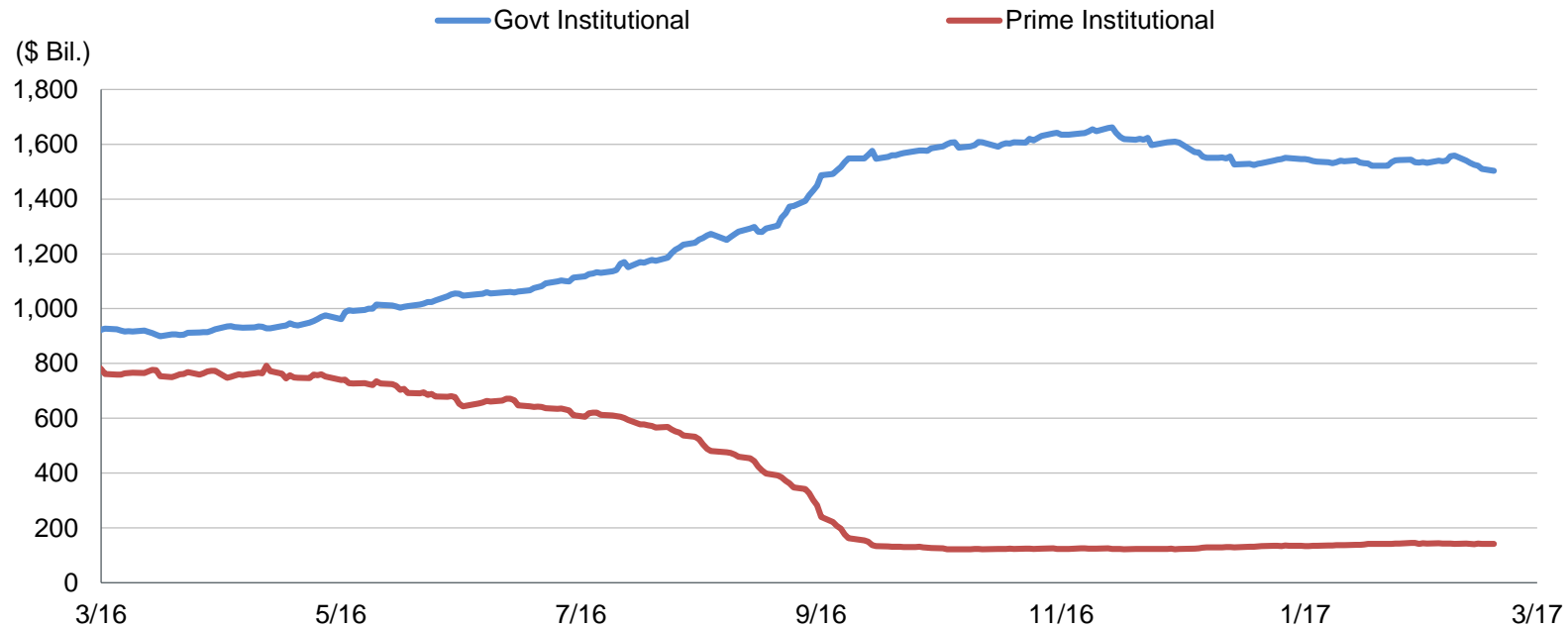
Instrument	Before	After
Prime money funds	95	?
Treasury/government MMFs	92	88
Treasury bills – direct	90	85
Bank demand deposits	90	85
Ultra-short bond funds	80	80
Commercial paper – direct	75	70
SMA	60–80	55–75
Internally-managed portfolios	40–80	35–75

Source: Treasury Strategies' corporate clients' experience

# MMF Reform Created Significant Change in Short-term Markets

**Re-allocation to Government Funds:** Treasurers along with other investors moved almost \$870 billion out of prime funds as a result of money fund reform. Most utilized government funds as a safe and default option. In 2017, a raising interest rate environment could create shifts from government funds and spreads increase and investors decide on options.

**Funding Difficulties:** Flows from prime funds increasing costs of borrowing in the short-term market, particularly foreign banks.



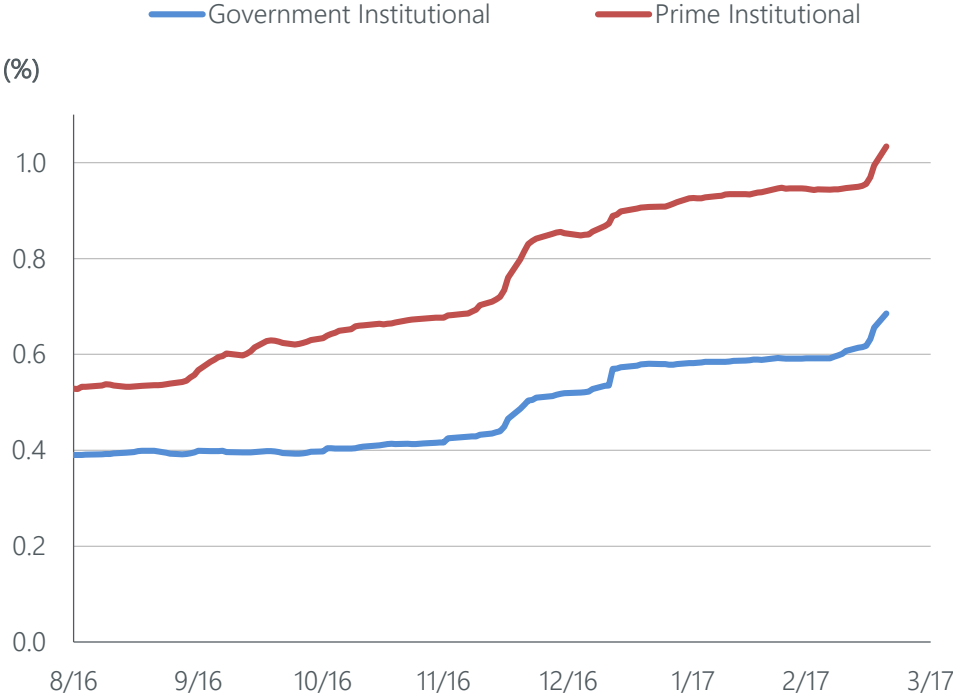
Source: iMoneyNet.



# Prime and Government Fund Yields Reflect Market Conditions

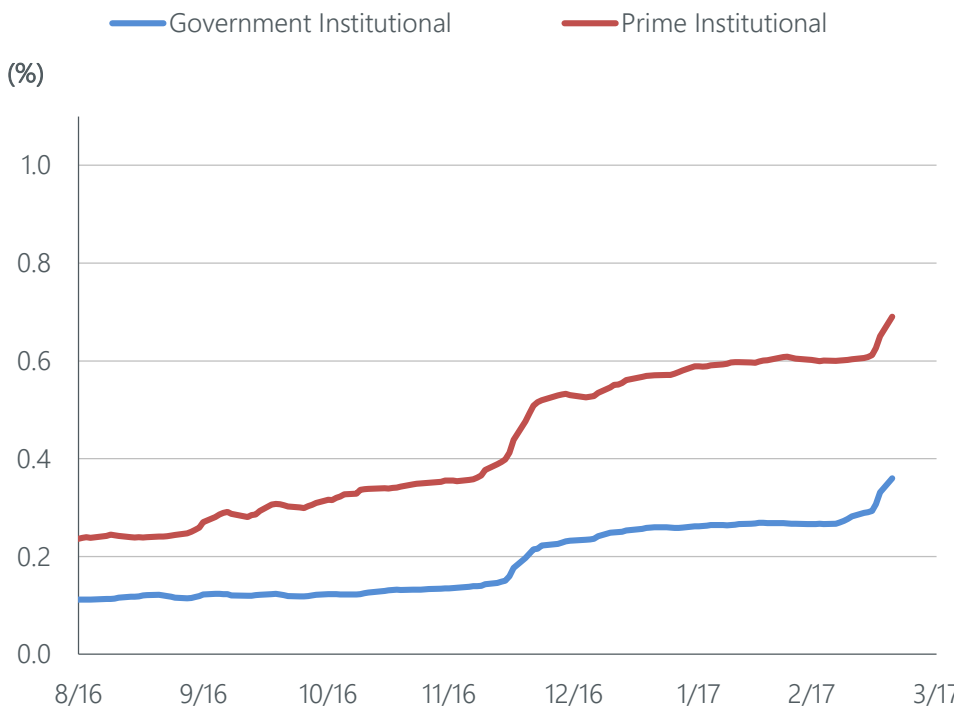
**Spreads Rise, Likely More After Rate Hike:** Prime funds normalizing portfolios post-reform, coupled with additional Fed rate hike can propel spreads higher. Spreads at 50 bps for a prolonged time may cause flow from government assets to prime.

**Money Market Funds 7-Day Gross Yields**



Source: iMoneyNet.

**Money Market Funds 7-Day Net Yields**



Source: iMoneyNet.

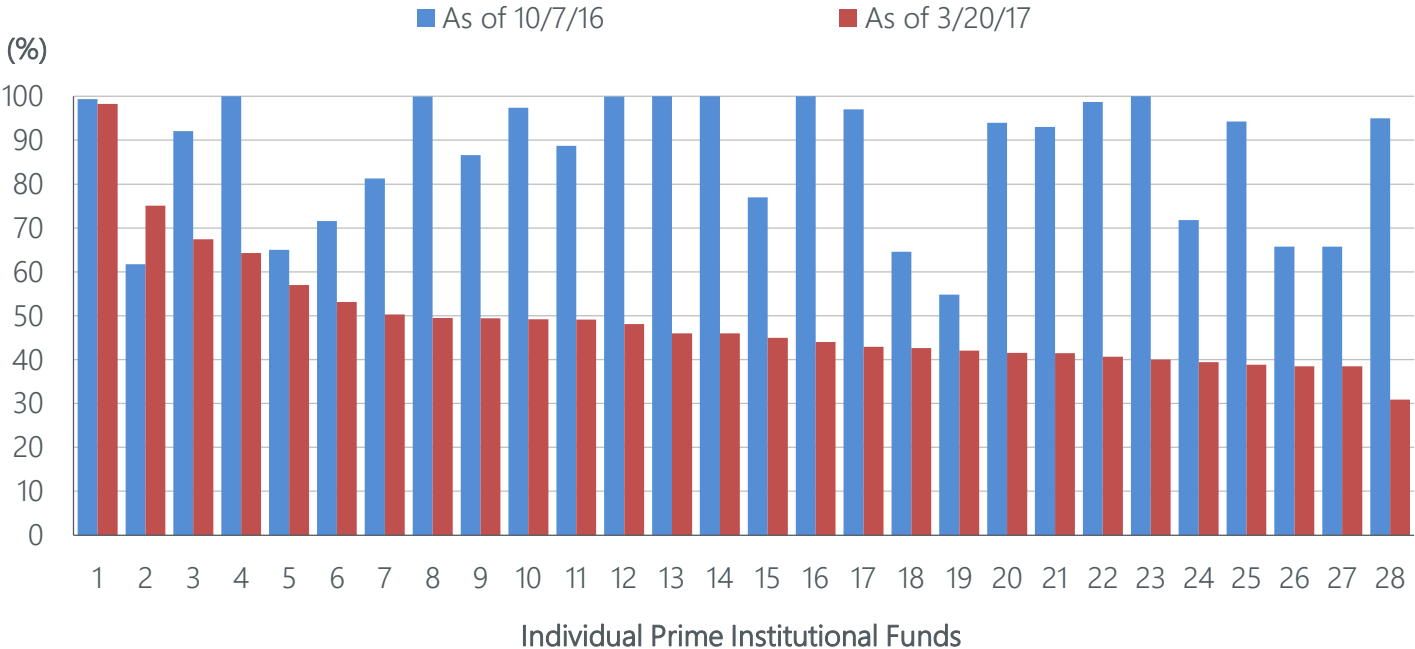
# Prime Institutional Money Fund Liquidity Declines for Most Funds

**Regulation drove liquidity to highest levels:** To prepare for outflows anticipated due to regulation effective date managers increase liquidity to far higher than regulatory thresholds or historical averages.

**Weekly Liquidity Down From Peak for 28 Prime Institutional Funds:** Weekly liquid assets now averaging 38%. Five funds below 40%.

**Range in weekly liquidity is large:** Currently there doesn't seem to be a market standard for weekly liquid assets with funds ranging from 40% to 100%. Investor composition can be a key factor influencing this decision.

Weekly Liquidity Down from Peak for 28 Prime Institutional Funds

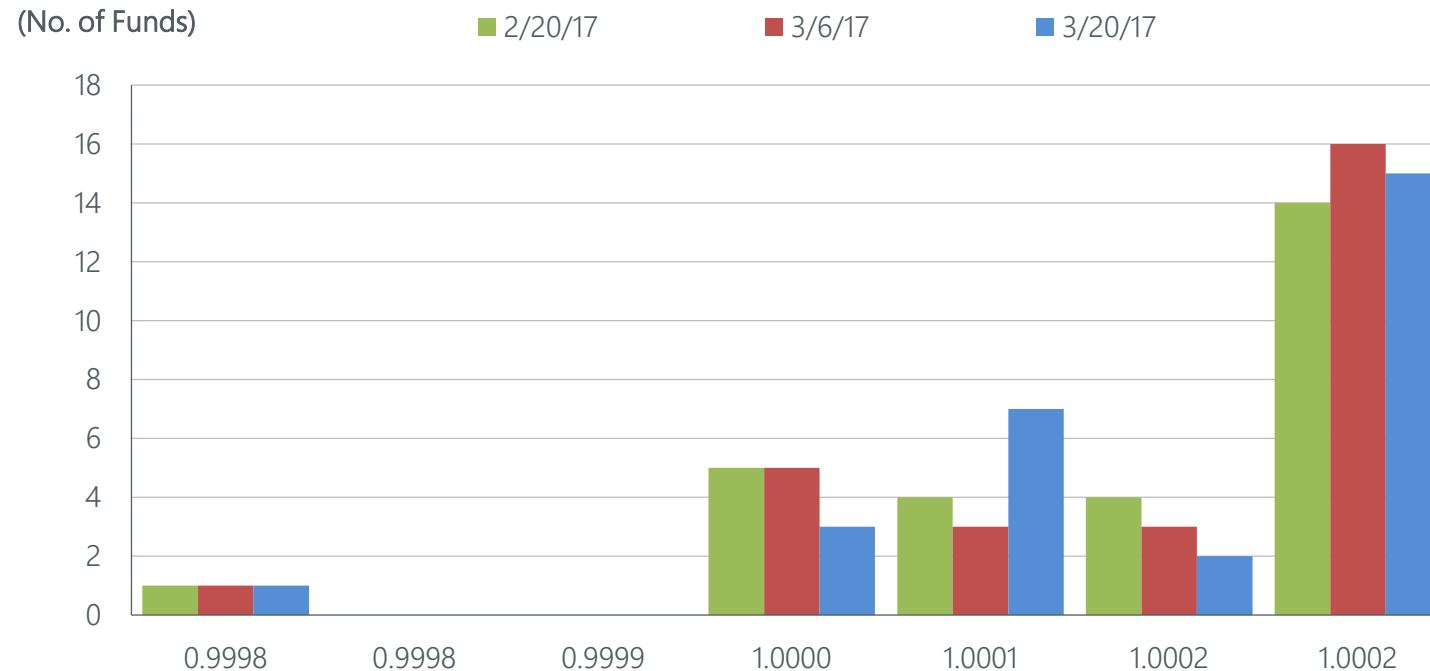


Source: Fitch, Crane Data.

# Review Institutional Prime Funds NAV Performance: Meet Investment Objectives?

**NAVs Near \$1, Consistent and Stable:** NAVs are very close to \$1 and changes are very small even as market reacts to increases in the Fed Funds Rate.

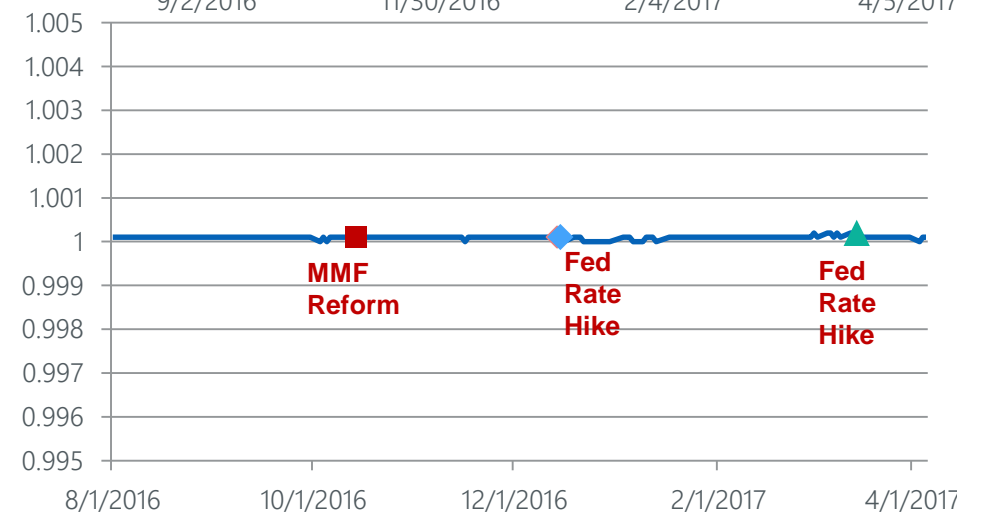
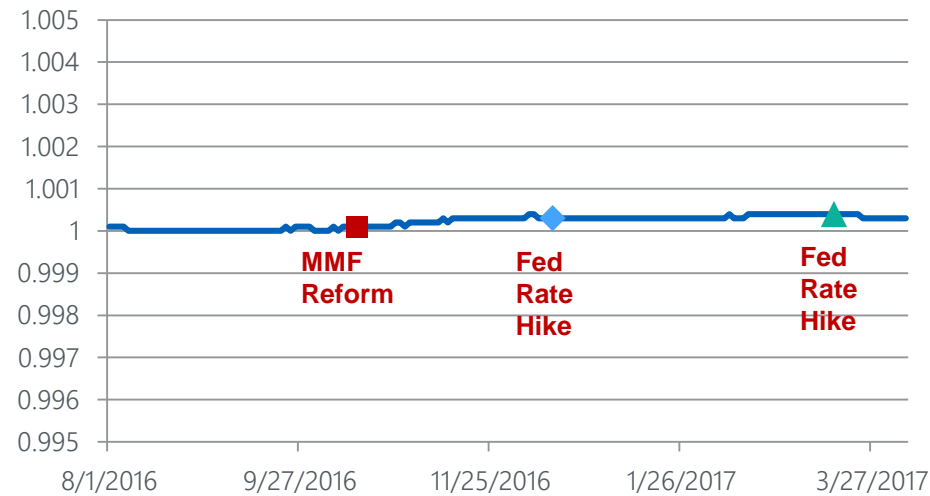
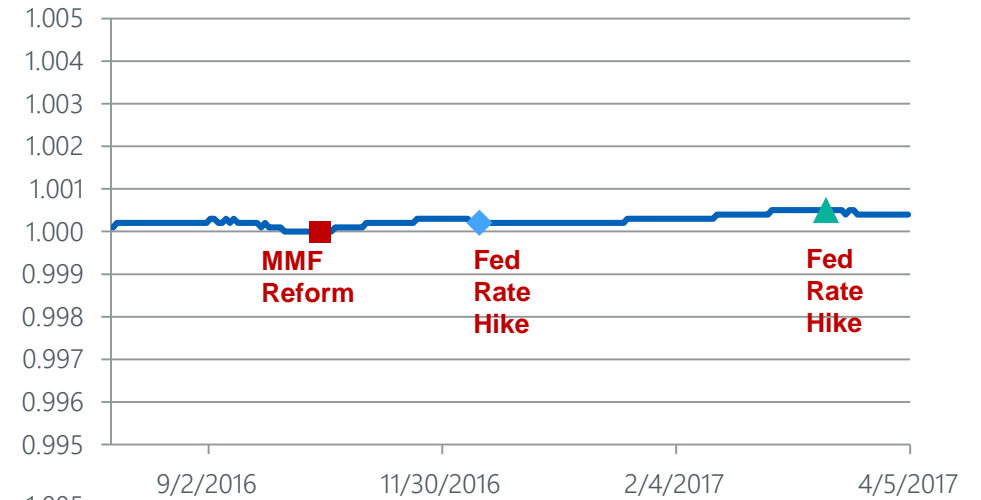
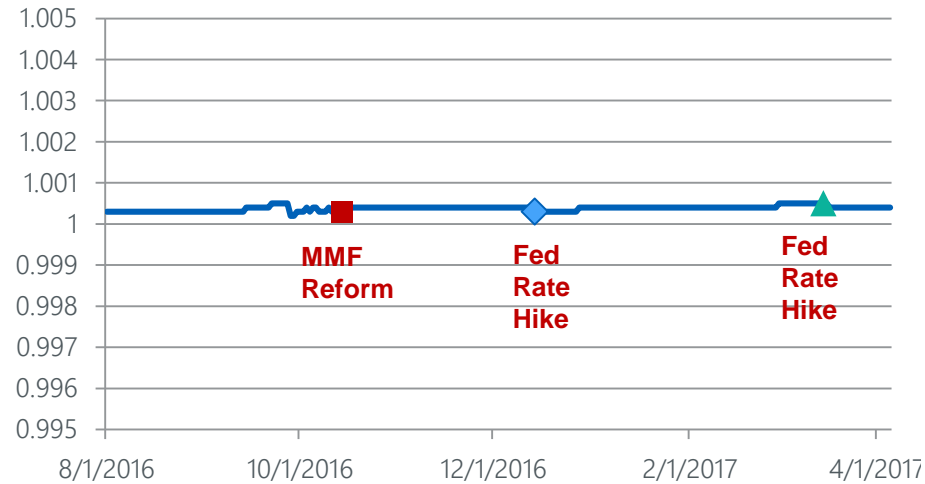
**Fitch's Rating Criteria for Prime MMFs Focuses on Portfolio Risks:** Primary rating factors for money funds and other liquidity products is to evaluate liquidity, credit, and market value risks in portfolios. Fitch's freely available MMF Rating Criteria provides valuable metrics that anyone can use to analyze funds.



Source: Fitch, Crane Data.

# Review Institutional Prime Funds NAV Performance: Meet Investment Objectives?

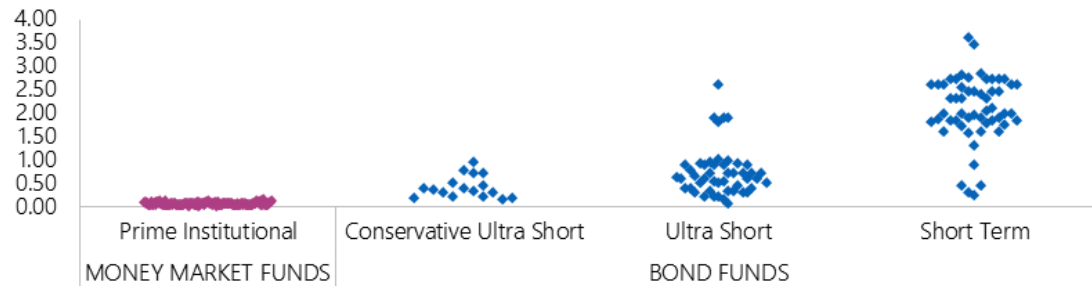
**NAV Volatility Minor Post-Reform:** NAVs for the four largest institutional prime MMFs show minor volatility.



# Review Alternative Products: Understand Varying Degrees of Risk Across New Investments

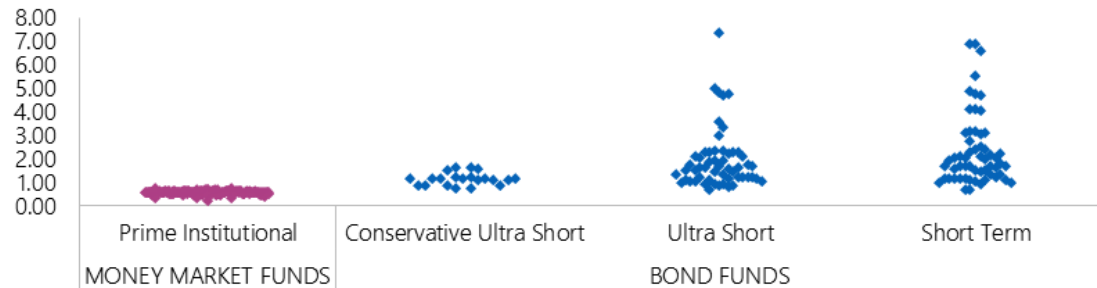
Structuring cash between strategic and operating is increasingly important when considering differing risk profiles of prime MMFs and short-term bonds.

## Duration



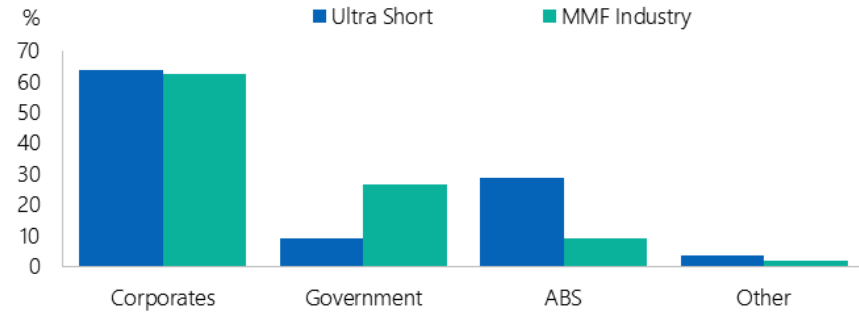
Source: Crane Data, Fitch Ratings

## Gross 30 Day Yield



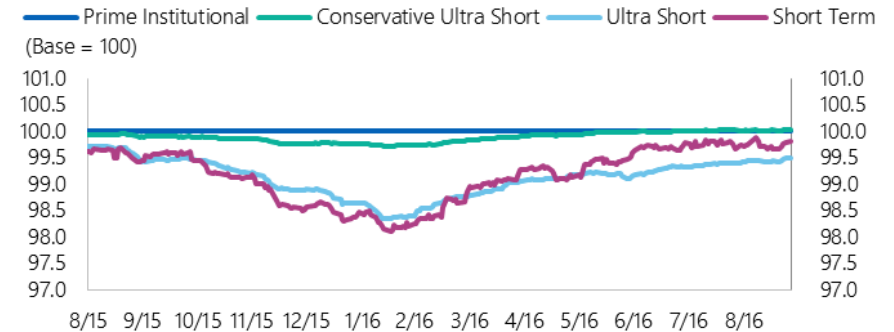
Source: Crane Data, Fitch Ratings

## Portfolio Composition



Source: Fitch, Crane data, fund fact sheets

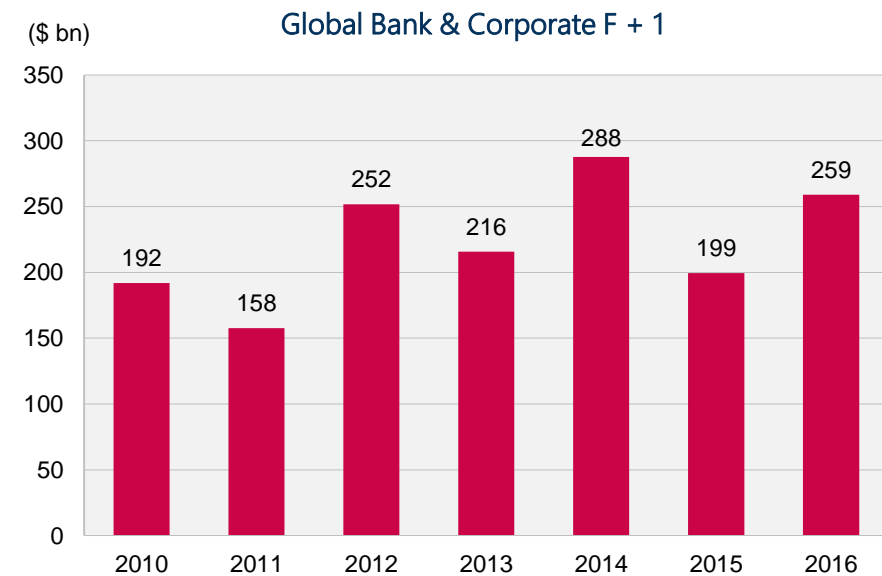
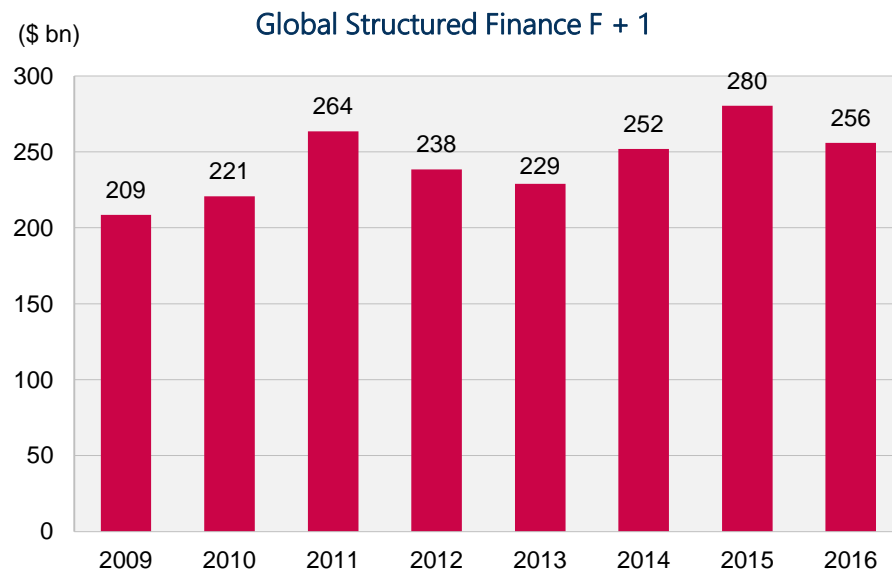
## NAV Volatility (Avg)



Source: Bloomberg, Crane Data, Fitch Ratings

# Review Investment Guidelines: The Markets Changed Dramatically, Keep Flexibility

- Investment flexibility and diverse credit views important. Perform a review of investment guidelines to ensure flexibility.
- \$2 trillion of global structured finance and \$1.6 trillion of global banks and corporate finance bonds issued with Fitch and one other rating (Fitch +1) since 2009. Investment guidelines that do not include Fitch ratings are a competitive disadvantage compared to peers due to less flexibility, less supply, less opportunities.



**Sample investment guidelines language:** “Investments must be rated A/A/A2 or higher on the long-term scale and/or F-1/A-1/P-1 or higher on the short-term scale by at least two of three said rating agencies (Fitch Ratings, S&P, or Moody’s). Money market funds must be rated equivalent of ‘AAA’ by at least two of three said rating agencies (Fitch Ratings, S&P, or Moody’s).”

# Review Investment Tools: Assess Portfolio Risks are Inline with Investment Goals

**Case study:** Investors are focused on money fund liquidity but not all MMF AAA ratings are the same at assessing this risk.

Which Approach is More Aligned with Your Concerns?

## Fitch AAmmf Rating

Liquidity Risk is Essential Component of Criteria

Money Market Fund Ratings (assigned to money market funds and other cash management products) are an opinion on a fund's capacity to fulfil its investment objectives of providing ready **liquidity and preserving principal**.



## S&P AAAM Rating

Does Not Address Liquidity Fees and Redemption Gates

“A money market fund rating is a forward-looking opinion about a fixed-income fund’s ability to **maintain principal value** (i.e. stable net asset value and to limit exposure to principal losses due to credit risk. We generally **do not lower ratings to ‘Dm’ when the manager of any fund suspends redemptions for up to five business days.**”

**Additionally, if a fund elects to impose a 2% redemption fee this is a “credit positive.”**

# Fitch Ratings: Strong Commitment to Short-term Market and Cash Management

## Industry Leading Research

- Money fund trends: bi-weekly update dashboard
- Special reports highlighting key themes
- Commercial paper dashboard
- Distribution dedicated to corporate treasurers

## Active Media Engagement

**Prime Money Funds Getting More Liquid Ahead of Reform.** *Shift toward on liquid assets suggests they are readying for a growing wave of redemptions over the next few weeks, according to Fitch Ratings.* –CFO Journal 9-14-2016

**Fed: Banks Cut Use of Short-Term Debt Ahead of New Money-Fund Rules** *In recent months, investors have moved more than \$800 billion out of such funds and into government funds, according to Fitch Ratings.* –The Wall Street Journal 10-6-2016

**Cash is No Longer Trash.** *Money-market funds have sharply increased payouts. Municipal-bond money funds, yielding more than 1%, are an especially good deal.* –Barron's 10-8-2016

**A \$1 Trillion Paradigm Shift Boosts Demand for U.S. Bills** *“This was a structural change,” said Gregory Fayvilevich, an analyst in the fund and asset management group at Fitch Ratings. “Prime money funds traditionally made up a very big portion of holders of CP. That is why you are seeing a very big impact.”* –Bloom 10-10-2016

[www.fitchratings.com/shortterm](http://www.fitchratings.com/shortterm) Research portal for treasurers.

**Short-Term Credit Markets**

Global Home > Short-Term Credit Markets

**RESOURCES**

- Asset-Backed Commercial Paper Scorecard
- Commercial Paper Headlines
- Commercial Paper Monitor
- Money Market Funds
- US IG Data Comparator
- US Money Market Fund Dashboard
- Whitepaper: Cash Management (PDF 4122 KB)

**CONTACTS**

**CORPORATES**

**Philip Zahn**

Analytical  
+1 312 606 2336

**FINANCIAL INSTITUTIONS**

**Bain Rumohr**

Analytical  
+1 312 368 3153

**FUNDS & ASSET MANAGERS**

**Greg Fayvilevich**

Analytical  
+1 212 908 9151

**FUNDS & ASSET MANAGERS**

**Roger Merritt**

Analytical  
+1 212 908 0636



# Contact Me



**Ian Rasmussen**

Senior Director

Fitch Ratings

212-908-0232

[ian.rasmussen@fitchratings.com](mailto:ian.rasmussen@fitchratings.com)

Fitch Ratings' credit ratings rely on factual information received from issuers and other sources.

Fitch Ratings cannot ensure that all such information will be accurate and complete. Further, ratings are inherently forward-looking, embody assumptions and predictions that by their nature cannot be verified as facts, and can be affected by future events or conditions that were not anticipated at the time a rating was issued or affirmed.

The information in this presentation is provided "as is" without any representation or warranty. A Fitch Ratings credit rating is an opinion as to the creditworthiness of a security and does not address the risk of loss due to risks other than credit risk, unless

such risk is specifically mentioned. A Fitch Ratings report is not a substitute for information provided to investors by the issuer and its agents in connection with a sale of securities.

Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch Ratings. The agency does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security.

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS AND THE TERMS OF USE OF SUCH RATINGS AT [WWW.FITCHRATINGS.COM](http://WWW.FITCHRATINGS.COM).

## New York

33 Whitehall Street  
New York  
NY 10004

## London

30 North Colonnade  
Canary Wharf  
London, E14 5GN