Cash management's hot buttons

NOW IN ITS SEVENTH YEAR, JPMORGAN ASSET MANAGEMENT'S GLOBAL CASH MANAGEMENT SURVEY, CONDUCTED IN CONJUNCTION WITH THE ACT, CONTINUES TO PROVIDE CORPORATE TREASURERS AND OTHER CASH INVESTORS WITH VITAL INFORMATION ON THE LATEST TRENDS AND THEMES IN THE CASH MANAGEMENT INDUSTRY. **ROBERT DEUTSCH** REPORTS.

Executive summary

- **Three major cash management themes emerge from the responses received: treasurers continue to demand high levels of security, the search for higher yields remains strong, and money market funds are increasingly seen as the most effective method for managing cash.**

With a record number of treasurers taking part, JPMorgan Asset Management's global cash management survey, conducted in conjunction with the ACT, continues to provide treasurers with valuable insights into how the industry is developing, the products that treasurers are currently using and the performance and service levels that are now demanded.

The global spread of respondents this year has been particularly impressive, with treasurers from a wide range of regions and markets helping to make the survey more globally inclusive than ever before. For the first time, we also welcomed the endorsement and support of the European Associations of Corporate Treasurers (EACT) for this research.

The survey's questions also continue to evolve as we strive to provide even more insightful analysis. This year, for example, we delved deeper than before into the minimum credit ratings and targeted returns that corporate treasurers require when investing their surplus cash, distinguishing for the first time between direct investments and money market fund investments.

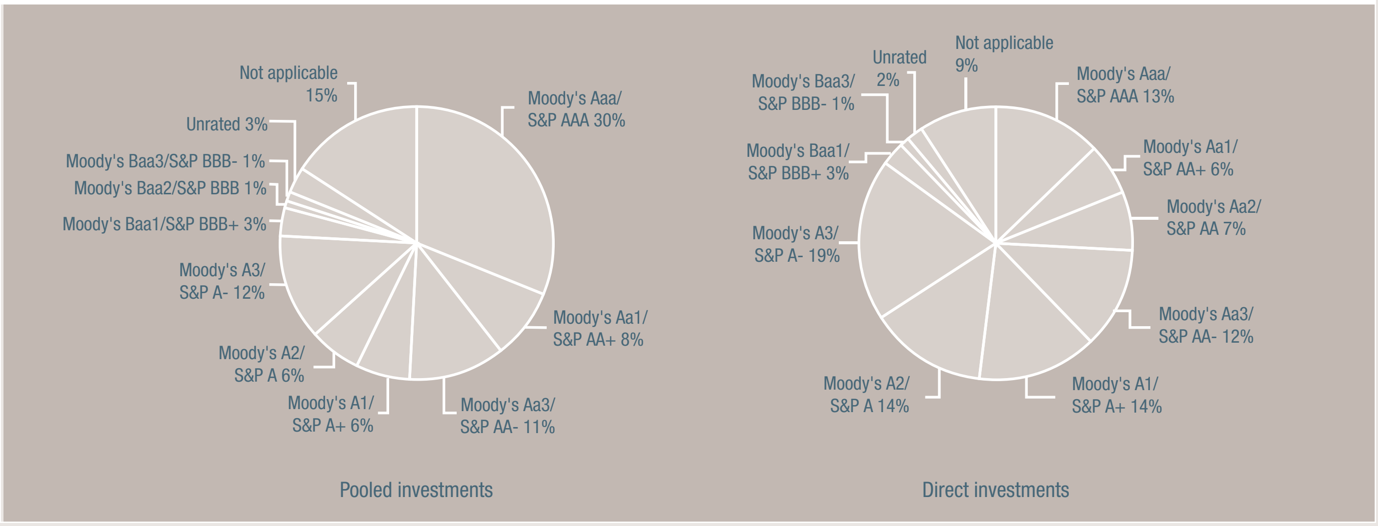
SECURITY The survey shows that treasurers continue to demand investment-grade credit ratings for their cash investments, with very few respondents prepared to invest in securities or funds with a credit rating below BBB.

The desire for security appears to have become even stronger recently, with a big fall recorded in the number of treasurers prepared to invest in unrated securities or funds. This year, for example, just 3% said they invested in unrated money market funds, compared with 27% of treasurers in the 2003 survey (see *Figure 1*).

The fall in demand for unrated funds doesn't appear to have been caused by any change in investment guidelines – more than a quarter of respondents with investments in money market funds said they could invest in unrated funds if they wanted to.

Perhaps the increase in risk aversion may be due to concerns over rising interest rates. Certainly, higher rates, particularly in the UK and

Figure 1. Minimum credit rating required



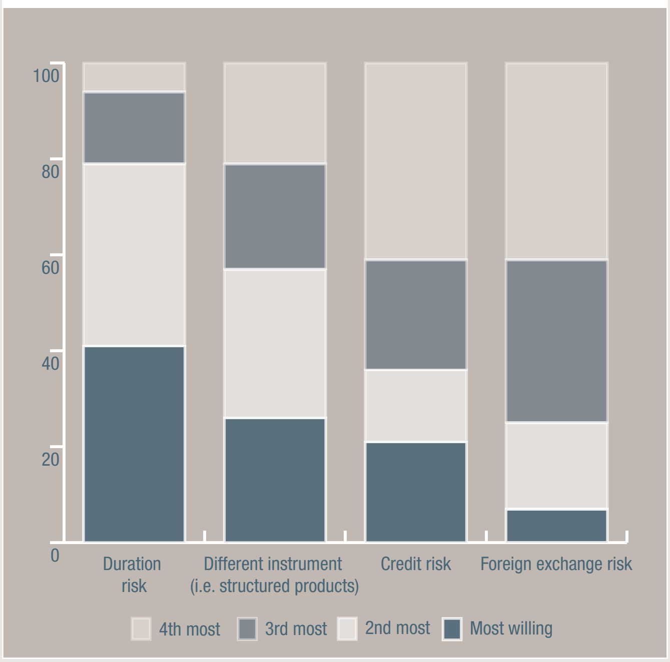
the US (and now also in Europe), mean that treasurers can get more respectable returns on their cash deposits without reducing the quality of their investments.

YIELD The survey's results show that, although treasurers continue to target a higher credit rating on their cash investments, they also continue to target high returns. More than a quarter of treasurers globally, according to the survey, are looking for returns in excess of London Interbank Offered Rate (Libor), although the majority seem to target London Interbank Bid Rate (Libid). These return expectations were similar for treasurers investing directly and for those using money market funds.

However, treasurers are unwilling to increase credit risk in order to boost potential returns despite their clear desire to obtain competitive returns. Only 21% of respondents to the survey said they would be willing to increase credit risk to boost performance. This unwillingness could be due to investment guideline restrictions, but the current rising interest rate environment in the US and Europe may be causing treasurers to rein in their risk budgets.

Instead of lowering the credit quality of their portfolios, treasurers are investing their cash for longer to improve potential returns, with some 41% of respondents saying that they were willing to invest over longer time periods in order to increase yields. This willingness to invest for a longer time horizon is reflected in an increase in the usage of yield-enhanced funds, which have a slightly longer average duration than standard AAA-rated liquidity funds, allowing them to target higher returns (see *Figure 2*) .

Figure 2. Willingness to take risk for higher yields



MONEY MARKET FUNDS Another key survey finding was the continuing growth in popularity of money market funds as a cash management tool at the expense it seems of bank deposits. Although bank deposits are still used by most treasurers (51%), the figure is down from last year's survey, where they were used by 67% of respondents, and much lower than the 72% recorded in the 2003 survey.

On average, treasurers allocate 51% of their surplus cash to bank deposits, 20% to direct investments and 29% to pooled investments. There were some regional differences, with US respondents using significantly more direct investments (37%) and pooled investments (48%) than European or Asian-based respondents. The greater use of pooled investments, such as money market funds, in the US is unsurprising, given that bank deposits are not regularly used by US investors for their cash investments. Instead, US cash investors have traditionally used money market funds for their excess cash requirements (see *Figure 3*).

Across all regions, however, the growing appetite for money market funds is evident from the survey's results. For example, we asked treasurers not using pooled investments if they would consider them in the future. Of those that were considering investing in pooled funds, money market funds were most popular, at 72%. Yield-enhanced funds also look set for increased usage in the future, with more than a third of respondents saying they were considering investing in these products, even though only 3% of respondents were currently allocating cash to them.

OTHER KEY FINDINGS A focus on security, yield and the growing usage of money market funds stood out from the survey's findings. But other results and trends also make interesting reading for treasurers.

For example, the survey reveals that the move towards global cash management structures continues to gain pace at the expense of regional management. 28% of respondents said they managed cash globally, and 36% said they managed cash regionally with global oversight, compared with just 13% who managed cash regionally, 10% who managed cash locally with regional oversight and 13% who managed cash with local autonomy (see *Figure 4*).

When looking at future intentions, the trend towards global cash management becomes even clearer. If respondents' predictions are accurate, the survey suggests that in the future only 11% of treasurers will have cash management structures that allow for some level of local autonomy.

Another notable finding concerns the use of investment sweeps. This year's survey reveals that fewer treasurers are using automated sweeping compared with 12 months ago. However, the decline is particularly marked in the case of subsidiary companies, which suggests it could simply be a function of the centralisation of cash management processes, bringing subsidiary companies in line with the actions of the parent company. This certainly would be consistent with the move towards global cash management structures noted earlier.

WHAT DOES THE FUTURE HOLD? The survey asked respondents about their key cash management concerns for the future, whether they thought external providers could be doing anything differently to assist them, and what they thought the key developments would be in the industry over the next five years.

In terms of concerns, the ability to improve cashflow forecasting was mentioned by several respondents, particularly as a way of improving yields while maintaining the highest credit quality. These responses are certainly consistent with the desire for security and yield expressed throughout the survey.

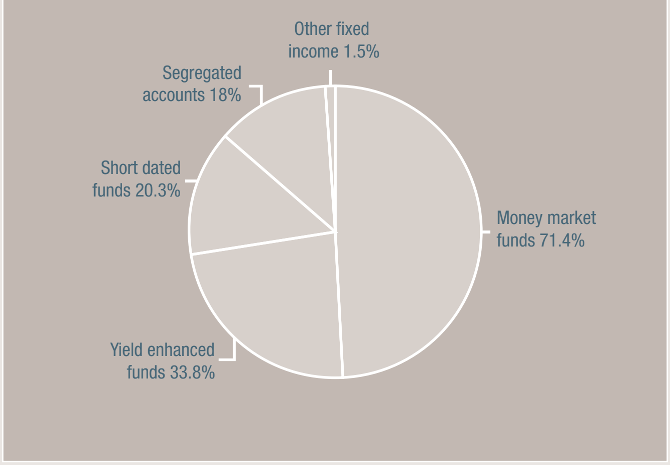
Treasurers gave many suggestions for how external providers could improve their services. Among these suggestions, it is clear that treasurers are looking for flexible products, in terms of cut-off times, fees and services offered, and simpler, more effective systems and portals.

A theme which emerges from the answers we received on future industry developments was the belief that automated and internet-based solutions would become the norm for cash management going forward.

On behalf of JPMorgan, I would like to thank everyone who participated in the global cash management survey, as well as the ACT for its ongoing support and the EACT, which endorsed the survey for the first time this year.

Robert Deutsch is Head of Global Cash at JPMorgan Asset Management.
www.jpmorgan.com
The complete survey can be found on the JPMorgan Asset Management website at:
www.jpmorgan.com/assetmanagement/liquidity
or on the ACT website at:
www.treasurers.org
To obtain a hard copy of the survey, please contact JPMorgan Asset Management by calling 020 7742 5805.

Figure 3. Instruments being considered for use



THE DESIRE FOR SECURITY APPEARS TO HAVE BECOME EVEN STRONGER RECENTLY, WITH A BIG FALL RECORDED IN THE NUMBER OF TREASURERS PREPARED TO INVEST IN UNRATED SECURITIES OR FUNDS.

Figure 4. How cash management is and will be structured