Risk back on the table

JIM FUELL PREVIEWS THE KEY FINDINGS OF THIS YEAR'S J.P. MORGAN GLOBAL LIQUIDITY INVESTMENT SURVEY, WHICH POINT TO A CONTINUED RECOVERY IN RISK APPETITE AMONG TREASURERS.

The J.P. Morgan Global Liquidity Investment Survey provides a unique barometer of corporate cash investment trends around the world. Now in its 13th edition, the survey (formerly known as the J.P. Morgan Global Cash Management Survey) has provided a benchmark for corporate treasurers since 1999, tracking short- and longer-term shifts in attitudes and behaviours in liquidity investment.

The 2011 survey is the most comprehensive yet, with a record 487 treasurers from around the world providing their views by online questionnaire between July and September. Once again, the survey was conducted with the help and support of the ACT.

GLOBAL RESPONSE The 2011 survey maintained a truly global focus, with treasurers responding on behalf of organisations across a wide range of regions and markets. This year saw a greater proportion of responses from Asia (20%, up from 11% in 2010) and EMEA (45%, up from 31%), as well as continued strong participation from North America (see Figure 1).

As always, the survey sought to capture the views of treasurers from organisations of all sizes, from the largest multinationals to the smaller regional players. This year, around one in six respondent organisations had a market capitalisation of under $500m, while 37% were valued at more than $5bn. Respondents represented companies and organisations from all sectors, from industrials and technology to financial services and healthcare.

DELVING DEEPER The wide geographical spread and broad industry coverage means the 2011 survey is one of the most informative to date. It also provides a valuable insight into the investment strategies and policies of corporate treasurers in today's volatile markets.

The full survey report is still being compiled and will be available in December. Initial findings suggest that the recovery in risk appetite witnessed in the 2010 survey has continued, with treasurers starting to overcome the extreme caution of recent years and increase their focus on yield. However, the financial crisis appears to have had an enduring effect on attitudes and behaviours among treasurers, and security remains key. While treasurers are increasingly well equipped to deal with risk, they are perhaps less prepared for regulatory challenges in the coming years.

EXTREME CAUTION CONTINUES TO RECEDE AND TREASURERS ARE REFOCUSING ON THE RETURNS THEY CAN OBTAIN FROM SURPLUS CASH.

CONTINUING RECOVERY IN RISK APPETITE The 2011 survey took place against a backdrop of renewed volatility on global financial markets, as the euro zone debt crisis escalated, the US credit rating was downgraded and fears mounted that the world may be heading back into recession. Nonetheless, the findings suggest that risk appetite among corporate treasurers continues on the path of recovery noted in last year's survey.

Last year, the beginnings of a recovery from the extreme risk aversion of the financial crisis were evident in a change in the returns treasurers were looking for from their cash investments. In 2009, the majority of treasurers were content to receive returns in line with

Figure 1: Survey respondents by location of main treasury centre

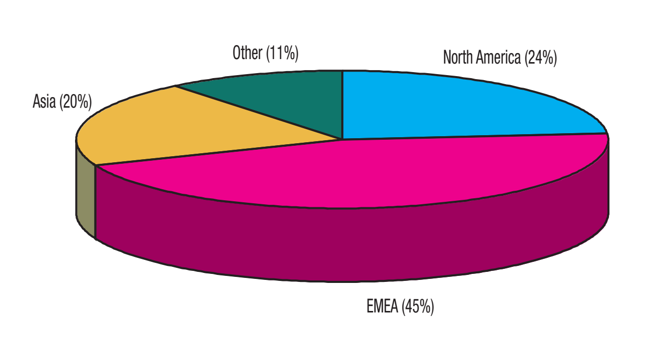


Figure 2: Target returns from short-dated cash

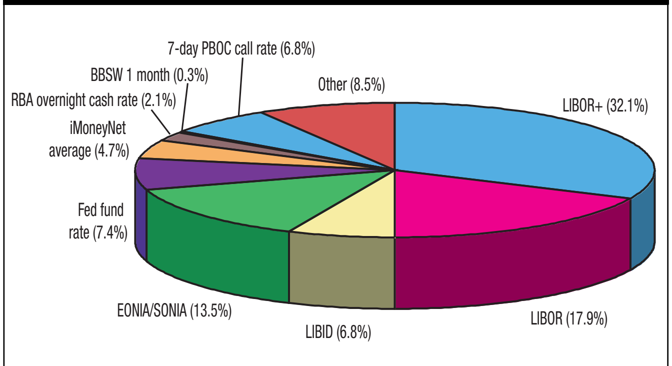
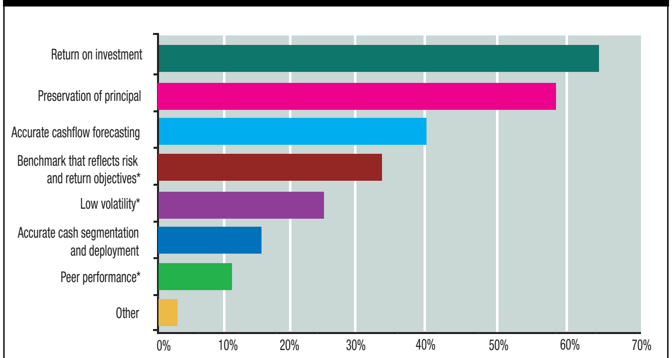


Figure 3: Measuring investment success



*Base = 447. 'Other' included FX losses, liquidity, FFP/interest, return on risk. *New choices this year.*

Figure 4: Areas of importance in the treasury department today

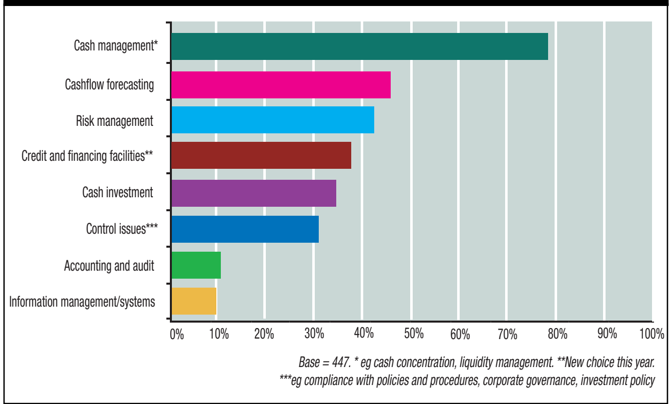
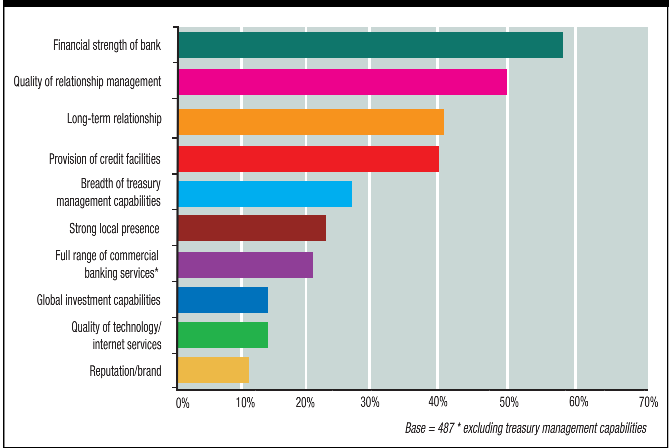


Figure 5: Criteria for choosing a primary bank



LIBOR from their surplus cash, with findings throughout the survey suggesting that the emphasis was on security rather than yield. In 2010, however, the most commonly selected return preference, at 27%, was LIBOR+. This year LIBOR+ was selected by 32% of treasurers, suggesting that extreme caution continues to recede and treasurers are refocusing on the returns they can obtain from their surplus cash (see Figure 2).

After several years of extremely low yields, treasurers are perhaps becoming frustrated, and this is evident in an increased willingness to take on risk. Last year, the majority of respondents who wanted higher yields were not prepared to take on additional risk to achieve them. In contrast, this year only 44% are unwilling to take on more risk, and an increased proportion of treasurers are willing to take on all types of risk, including credit and liquidity risk. As in 2010, duration extension is the most popular additional risk treasurers are willing to take in an effort to boost yields.

Elsewhere in the survey, a recovery in confidence and an increased appetite for yield are evident. In 2010, when treasurers were asked how they measure investment success, the most selected answer was preservation of principal, closely followed by accurate cashflow forecasting. Return on investment was in third place, selected by just 48% of respondents. This year, return on investment has leapfrogged into first place, and was chosen by 64% (see Figure 3). Preservation of principal is second, and cashflow forecasting a distant third.

THIS YEAR'S FINDINGS SUGGEST THAT TREASURERS ARE MAINTAINING THEIR FOCUS ON LIQUIDITY AND SECURITY, EVEN AS THEY BEGIN THEIR QUEST FOR HIGHER YIELDS.

CAUTION PERSISTS Nonetheless, the lessons of the crisis will not be easily forgotten, and treasurers maintain their focus on liquidity, credit quality and counterparty stability. This year, as in 2010, when treasurers were asked to comment on the key concerns in their treasury departments today, the most selected response was liquidity, with the majority of treasurers (65%) identifying it as one of their top five concerns.

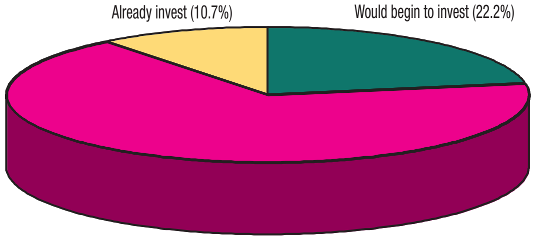
In some parts of the survey, the emphasis on risk management and security was even more evident this year than last, suggesting that treasurers are continuing to change their attitudes and behaviours in the wake of the crisis. When treasurers were asked to identify the top three areas of importance in the treasury department, the top two responses were unchanged from 2010, with cash management in first place and cashflow forecasting in second (see Figure 4). However, there has been a significant increase compared with both 2010 and 2009 in the proportion of treasurers viewing risk management as a key area of importance, and it has moved from fifth place last year to third this year.

Furthermore, when selecting a primary bank, the most important criterion for treasurers is now the financial strength of the institution, which has overtaken the quality of relationship management for the first time, and with a clear margin (see Figure 5). This perhaps reflects a renewed concern over the stability of banks as a result of the debt crisis in the euro zone. Reputation/brand remains a relatively marginal concern, but it is interesting to note that the proportion of treasurers selecting this criterion has doubled since last year.

The responses to this question differed markedly by region. In Asia, strong relationships remain paramount, with the quality of relationship management taking the top spot ahead of financial strength, and long-term relationships valued more highly than in any other region. However, financial strength is most important among treasurers in North America, and was also the most selected response in EMEA.

PREPARING FOR REGULATORY CHANGE This year, the survey included some new questions designed to investigate attitudes among treasurers to potential regulatory change that may impact liquidity investment management, particularly regarding pooled investments. Bob Deutsch, head of global liquidity at J.P. Morgan Asset Management, said: "Since the financial crisis, there has been significant debate within the fund industry and from regulators on how to mitigate systemic risk in short-term investment vehicles. This debate has already led to various regulatory changes, such as the introduction of a two-tier approach to money market fund classification in Europe, and there is potential for further developments.

Figure 6: Willingness to invest in fluctuating NAV MMFs



"One aspect of the debate has centred around whether the elimination of the stable net asset value [NAV] element of money market funds would address the vulnerability of funds to mass redemptions (or 'runs') such as those experienced by prime money market funds in September 2008 after the Reserve Primary Fund 'broke the buck'. We addressed this issue in the survey this year, with interesting results."

According to the survey, 48% of treasurers use AAA-rated stable NAV money market funds (MMFs), 29% use AAA-rated stable NAV Treasury MMFs, and 12% use other short-dated fixed income funds.

To assess the attitude of treasurers to the importance of the stable NAV, we asked whether treasurers would consider using fluctuating NAV funds if stable NAV funds were no longer available. 22% said they would begin to invest in fluctuating NAV funds and 11% already do, but 67% said they would not, suggesting the stable NAV is highly valued (see Figure 6).

So far, treasurers appear relatively sanguine about potential regulatory changes, with only 6% citing regulation as the largest challenge they face in the coming year. However, as the responses to the question about willingness to invest in fluctuating NAV funds suggest, treasurers may be affected more than they perhaps imagine should some of the proposed changes come into effect.

IN SHORT The survey has once again taken the pulse of treasurers around the world. This year's findings suggest that treasurers are maintaining their focus on liquidity and security, even as they begin their quest for higher yields. A new challenge may emerge for treasurers in the form of changes to regulation in the MMF industry, and it will be interesting to see how these changes are reflected in the survey in the coming years.

For more detail on all the results from this year's survey, and for the final report, which will be available from December, visit www.jpmgloballiquidity.com

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