A Postmodern Paradigm for Corporate Cash Management

Deborah Cunningham
Executive Vice President
Federated Investors

Nancy L. Edwards, CTP
Treasurer
Metropolitan Washington Airports Authority

Kathleen Clune
Assistant Vice President
Pacific Life Insurance Company
The Liquidity Market:  
A Money Fund Manager’s Perspective

Deborah Cunningham  
Executive Vice President  
Federated Investors
Looking Back

• 2007 – Market focus on liquidity
• 2008 – Market focus on credit
• 2009 – Market focus on low yields
• 2010 – Reversal of quantitative easing
Quantitative Easing: Are We Done Yet?

- Discount rate raised from 0.50% to 0.75% on 2/19/10
- Completion of Fed purchase programs
- FRBNY Reverse Repo with Primary Dealers
- FRBNY Reverse Repo with Non-Traditional Counterparts – i.e., Money Market Funds
New World, New Oversight

- FRBNY Tri-Party Repo Working Group
- Liquidity Exchange Bank
- Rule 2a-7 reviewed and reworked
## Changes to Rule 2a-7

<table>
<thead>
<tr>
<th>Portfolio Quality</th>
<th>New or existing</th>
<th>Can money market funds implement immediately?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Second Tier ≤ 3%</td>
<td>Enhancement of existing requirement</td>
<td>Yes</td>
</tr>
<tr>
<td>Designated NRSROs</td>
<td>New</td>
<td>Yes, Board approval required</td>
</tr>
</tbody>
</table>
## Changes to Rule 2a-7

<table>
<thead>
<tr>
<th>Portfolio Maturity</th>
<th>New or existing</th>
<th>Can money market funds implement immediately?</th>
</tr>
</thead>
<tbody>
<tr>
<td>WAM Max 60 Days</td>
<td>Enhancement of existing requirement</td>
<td>Yes</td>
</tr>
<tr>
<td>WAL Max 120 Days</td>
<td>New</td>
<td>Yes</td>
</tr>
</tbody>
</table>
## Changes to Rule 2a-7

<table>
<thead>
<tr>
<th>Portfolio Liquidity</th>
<th>New or existing</th>
<th>Can money market funds implement immediately?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Illiquid Securities ≤ 5%</td>
<td>Enhancement of existing requirement</td>
<td>Yes</td>
</tr>
<tr>
<td>Minimum Daily Liquidity 10%</td>
<td>New (taxable funds)</td>
<td>Yes</td>
</tr>
<tr>
<td>Minimum Weekly Liquidity 30%</td>
<td>New</td>
<td>Yes</td>
</tr>
<tr>
<td>Know Your Client Procedures</td>
<td>New</td>
<td>Yes</td>
</tr>
</tbody>
</table>
## Changes to Rule 2a-7

<table>
<thead>
<tr>
<th>Stress Testing</th>
<th>New or existing</th>
<th>Can money market funds implement immediately?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stress:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Interest rates</td>
<td>New</td>
<td>Yes</td>
</tr>
<tr>
<td>– Cash flow</td>
<td></td>
<td>Board reporting required</td>
</tr>
<tr>
<td>– Downgrade or default</td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Spreads</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## Changes to Rule 2a-7

<table>
<thead>
<tr>
<th>Improve Operations</th>
<th>New or existing</th>
<th>Can money market funds implement immediately?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fund Liquidation: Board permitted suspension of redemptions if liquidating</td>
<td>Revision of existing authority</td>
<td>No</td>
</tr>
<tr>
<td>Ability to process transactions at price other than $1</td>
<td>New</td>
<td>Yes</td>
</tr>
<tr>
<td>Exemption for Affiliate Purchases – SEC notice, not permitted</td>
<td>Enhancement of existing practices</td>
<td>Yes</td>
</tr>
</tbody>
</table>
Adoption of New 2a-7 Rules: What To Expect When

- **5/5/10** - Overall rule effective date
- **5/28/10** - Compliance required for quality, individual security maturity, liquidity and repo changes
- **6/30/10** - Compliance required for weighted average maturity and weighted average life changes
- **10/7/10** - Compliance required for monthly portfolio Web site disclosures
- **12/7/10** - Compliance required for monthly reporting to SEC of mark-to-market NAV and other portfolio details (to be published by the SEC on a 60-day lag)
- **12/31/10** - Compliance required for NRSRO disclosure
- **10/31/11** - Compliance required for processing transactions at other than $1 NAV
Looking Ahead

- Further steepening of the yield curve anticipated
- Rates have bottomed
- Money market fund yields lag
- Reversal of quantitative easing continues
- Actual fed tightening begins
- Economic slow-growth allowing for slow and steady rate increases
Money Funds in Corporate Cash Management:  
*Do they – can they – work together?*
Tales from the Front Lines:

Nancy L. Edwards, CTP
Treasurer
Metropolitan Washington Airports Authority

Kathleen Clune
Assistant Treasurer and AVP
Pacific Life Insurance Company
A Look Back

• Prior to the fall of 2008
  – Is my fund rated?
  – Government and Treasury funds
  – “All fund managers are professionals”
  – Some funds better than others?
My Awakening

- Fall 2008 through 2009
  - Reserve Fund “broke the buck”
  - Am I earning any interest? (and how I found out)
  - Attended the Crane Money Fund Symposium
    - Fund Managers are professionals
    - Money Funds are a BIG deal
New World, More Due Diligence

• Match investment policy
  – Verify by reviewing fund holdings
• Verify ratings on funds
• Closer look at yields
• Review fund managers – not all are created equal
Our Outlook Today…and Down the Road

• Increased awareness of the relationships between security issuers, fund managers, fund purchasers
• Theme at Crane Symposium 2010
  – Funds’ supply problems
• Watching discussion on floating NAV
Past Practice

• Selected funds based on relationships
• Used rated prime funds only
• Daily investments based on rate of return
• No caps on level of investment
Reality Strikes Back (and Hard)

• Watched a hybrid institutional liquidity fund collapse
• Queried by senior management and board of directors on stability of vehicles
• Conference calls with all investment managers
• Cash became King!
Current Issues We Face

• Diversification in and out of funds
• Importance of fund as an investment vehicle
• Floating NAV – My opposition
• Liquidity is King!
Moving Forward

• More independent research
• Quality reviews
• Due diligence at portfolio level of funds
• Cap in funds
• Smaller stable of investable funds