




Association for
Financial Professionals®

2010 AFP Liquidity Survey Report of Survey Results

Underwritten by

 Promontory
Interfinancial Network, LLC
provider of  

2010 AFP Liquidity Survey

Report of Survey Results

June 2010

Underwritten by



**Association for
Financial Professionals®**

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As the provider of the Certificate of Deposit Account Registry Service® – CDARS® – and other services, Promontory Interfinancial Network is pleased to sponsor the *2010 AFP Liquidity Survey*. With CDARS, a bank that belongs to our Network can offer a customer access to multi-million-dollar FDIC insurance coverage.

The survey makes one thing perfectly clear: safety and security are foremost on the minds of financial professionals. To paraphrase Mark Twain, financial professionals clearly remain more concerned with the return of their money than the return on their money. Three quarters of the 2010 survey respondents choose “safety of principal” as their organization’s key investment objective, compared to just two percent who choose “yield.” Moreover, the survey finds that bank deposits are the predominant short-term investment vehicle for respondents; a striking 42 percent of short-term investment balances are kept in bank deposits, compared to 25 percent two years ago. In addition, 43 percent of organizations say they held larger balances of U.S. cash and short-term investments in May 2010 than they did in late 2009. Finally, three out of ten financial professionals say they expect their organizations to increase their U.S. short-term cash and investment balances over the next 12 months.

The 2010 survey report concludes: “Bank deposits remain a safe and liquid place in which to invest and as economic conditions improve, it will be interesting to see when corporate investors shift from investment vehicles that are safe and liquid to those that may offer higher yield.”

It will, no doubt, be interesting to see the shift – when it comes. But in a financial world likely to be characterized by low yields and volatility for some time to come, it is not likely to occur soon. Until it does, financial professionals who are risk averse will find federally insured bank deposits to be a safe harbor they desire.

For Promontory, the best news in the 2010 survey is that 17 percent of the respondents say that they have placed deposits through CDARS – a gratifying sign that CDARS has become fully accepted by sophisticated investors.

I hope you will find the 2010 survey to be as interesting and insightful as I do. Promontory appreciates the opportunity to have worked with AFP and looks forward to doing so again.

Sincerely,
Alan S. Blinder
Vice Chairman
Promontory Interfinancial Network, LLC

2010 AFP Liquidity Survey

Introduction

The U.S. economy, at least in terms of growth in gross domestic product (GDP), turned the corner during the early months of 2010. The improving economic outlook is a significant departure from the sharp recession that impacted not only the U.S. but also much of the world. During the rapid deterioration of business conditions over the previous two years, global credit markets froze, resulting in both corporate and individual investors fleeing from investment vehicles that previously had been deemed safe havens for short-term investments. Because of the detrimental impact that in the financial sector turmoil and the deep recession had on their access to short-term credit, organizations were increasingly emphasizing protecting principal of their short-term investment portfolio. A number of them moved investments into ultra-safe investment vehicles, such as bank deposits, money market mutual funds and Treasury securities.

The question is when (and at what pace) organizations will begin to open up their short-term investment portfolios and seek not only safety, but also increased liquidity and yield. At the same time, will organizations continue to hoard cash—as many have in recent years—or will they begin to seek other uses for this cash; such as for share repurchases and long-term business opportunities (e.g., M&A activity, capital investments)?

In early May 2010, the Association for Financial Professionals conducted its fifth annual *Liquidity Survey* to provide financial professionals with an understanding of how organizations currently manage their short-term investment portfolios. This year's survey also explored the impact of the new Securities and Exchange Commission rules affecting money market funds. Through the end of May, the survey generated 337 responses, which are the basis of this report.

The 2010 AFP Liquidity Survey was underwritten by Promontory Interfinancial Network, LLC. The Research Department of the Association for Financial Professionals, which designed the survey questionnaire, analyzed the survey results and wrote/edited the report, is solely responsible for the content of this report.

Key Findings

Key findings of the *2010 AFP Liquidity Survey* include:

- A plurality of organizations increased their balances of cash and short-term investments in the six months leading up to May 2010.
 - During May 2010, 43 percent of organizations held a larger balance in U.S. cash and short-term investments than they did six months earlier.
 - Twenty-four percent of organizations carried smaller cash and short-term investment balances compared to six months earlier, while 33 percent of organizations had no significant change in their short-term investment balances.
 - Thirty percent of organizations that have non-U.S. cash and short-term investment balances indicate that these balances have increased over the same six months.
- Three out of ten financial professionals expect their organizations will increase their U.S. short-term cash and investment balances over the next 12 months.
 - Twenty percent of organizations expect to decrease their U.S. short-term investment balances over the next year while half expect little significant change.
 - Two-thirds of organizations with balances of non-U.S. cash and short-term investments indicate that they intend to maintain these balances at current levels over the next year.
- Three-quarters of organizations have a written policy that outlines acceptable short-term investment policies.
 - Seventy-five percent of organizations that have written cash investment policies review and update those policies on a regular basis.
- Organizations remain quite conservative in the strategies associated with their short-term investment portfolios.
 - Overall, organizations' investment policies allow for the use of an average 4.7 short-term investment vehicles, in addition to bank deposits. While this is an increase from the average of 4.1 vehicles reported in the 2009 survey, it remains well below the average of five years ago.
 - Eighty-three percent of organizations permit the use of Treasury bills while at least 60 percent of organizations permit the use of commercial paper, "pure" Treasury money market mutual funds and agency securities.
- Even though an organization's investment policy may allow for a greater number of investment vehicles compared to a year earlier, most organizations are actually using relatively few instruments on their actual "allowable" list. On average, organizations use 2.4 investment vehicles for their cash and short-term investment balance. While this matches the average of 2008, it is an increase from the average 1.6 instruments used in 2009.
 - Organizations allocate an average 74 percent of their short-term investment balances in three safe and liquid investment vehicles: bank deposits, money market mutual funds and Treasury securities.
 - Bank deposits are the dominant investment vehicle for short-term investment portfolios. Forty-two percent of all short-term investment balances are held in bank accounts. Just two year earlier, the percentage was 25 percent.

- Twenty-one percent of organizations use an electronic, multi-family trading portal to execute at least some of their short-term investment transactions.
 - Organizations using trading portals execute an average of 73 percent of their money market mutual fund transactions through the trading portal.

In addition to questions related to cash and short-term investments, the *2010 AFP Liquidity Survey* asked financial professionals about the impact that new SEC rules on money market funds (MMFs) may have on their organization's use of said funds.

- More than two out of five respondents indicate that the 60-day shadow net asset value (NAV) will have an impact on their organization's investment decisions in money market funds.
 - Twenty-seven percent of financial professionals anticipate either reducing or completely eliminating MMFs from their short-term investment portfolios because of a possibility of a NAV falling below \$1.
 - Another 16 percent of organizations plan to monitor their funds and will sell them should the NAV decline below \$1.
 - Large organizations, those that are net investors and those with investment grade ratings are more likely than smaller organizations, those that are net borrowers and those with non-investment grade ratings to indicate that they anticipate dumping MMFs from their short-term investment portfolios because of the possibility of a NAV falling below \$1.
- More than two out of five respondents—including at least half of respondents from smaller organizations and those that are net borrowers—indicate that their organization is “generally comfortable” with the changes to 2a-7 funds and as a result do not expect to modify their investment strategy as a result.
 - 30 percent of organizations anticipate diversifying their investment selections because of an expected decline in yield.
 - A quarter of respondents report that their organizations will continue to use MMFs but will reduce their level of exposure to the funds.

Holdings of Cash and Short-Term Investments

Even as the U.S. economy stabilized, most organizations continued to face a tight credit market. A plurality of organizations increased their cash and short-term investment balances during the six months leading up to May 2010. Forty-three percent of organizations held larger balances of U.S. cash and short-term investments in May 2010 than they did in late 2009. A slightly smaller percentage of organizations decreased their U.S. and non-U.S. holdings of cash and short-term investments compared to a year ago (and reported in last year's survey). Twenty-four percent are carrying smaller cash and short-term investment balances, while a third of organizations report no significant change in their short-term investment balances. In the *2009 AFP Liquidity Survey*, 42 percent of organizations reported that they carried larger cash and short-term balances over the previous year, while 28 percent reported carrying smaller balances.

Large organizations are more likely to have increased their cash and short-term investment balances than are smaller organizations. For 44 percent of organizations with annual revenues greater than \$1 billion, their cash and short-term holdings have increased since late 2009 compared to 38 percent of smaller organizations. Conversely, a greater percentage of smaller organizations (29 percent) than larger organizations (18 percent) have seen declining cash balances during the same period.

Organizations that are net investors are far more likely than net borrowers to have increased their cash holdings during the first months of 2010. Forty-eight percent of net investors expanded their cash holdings over the previous six months compared to 33 percent of organizations that are net borrowers. A similar relationship is seen in terms of an organization's rating: organizations with an investment grade rating are more likely than those with non-investment grade ratings to have increased their cash and short-term investment balances (44 percent versus 33 percent).

Thirty percent of organizations that have non-U.S. cash and short-term investment balances indicate that these balances increased over the six months between November 2009 and May 2010. More than three out of five of organizations (62 percent) indicate little significant change in their non-U.S. cash balances, while just eight percent report smaller non-U.S. balances.

Organizations that increased their cash holdings over the past six months attribute the increase to a greater focus on having sufficient cash on hand to "maintain operations and getting through the recession" and on "working capital improvement." More than half of organizations that have seen their cash balances fall over the past six months indicate that the decline was the result of a need to spend cash on maintaining operations and getting through the recession.

Change in Cash and Short-term Investment Balances Over the Past Six Months
(Percentage Distribution)

		All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
U.S.	Much larger	15%	15%	16%	14%	16%	17%	12%
	Somewhat larger	28	23	28	19	32	27	21
	No significant change	33	33	38	41	31	35	37
	Somewhat smaller	15	18	13	16	14	16	16
	Much smaller	9	11	5	11	7	5	14
Non-U.S.	Much larger	8%	5%	10%	4%	11%	9%	6%
	Somewhat larger	22	19	28	16	28	28	18
	No significant change	62	68	60	72	58	60	70
	Somewhat smaller	4	3	2	3	2	2	2
	Much smaller	4	6	*	5	1	1	4

As business conditions have stabilized in 2010, financial professionals indicate that their organizations are less likely to further increase cash balances over the next year. Looking forward, half of organizations do not anticipate altering the size of their cash and short-term investment holdings over the next year. Thirty percent of organizations anticipate growing their cash balances over the next year while 20 percent expect the balances will contract. In the 2009 survey report, 44 percent of survey respondents anticipated that balances would not change going forward.

Larger organizations and those that are net investors are slightly more likely than smaller organizations or net borrowers to report that they anticipate growing their cash and short-term investments balances over the next year. Thirty-three percent of organizations with annual revenues greater than \$1 billion expect that their cash holdings will expand over the next year compared to 30 percent of smaller organizations. Similarly, 33 percent of organizations that are net investors expect to increase their cash holdings over the next year compared to 29 percent of net borrowers that expect to do the same.

The difference was even more significant between organizations with investment grade ratings versus those with non-investment grade ratings. Twenty-nine percent of organizations with investment grade ratings expect to grow their cash and short-term investment balances over the next year compared to 37 percent of organizations with non-investment grade ratings that expect to do so. The difference is consistent with the findings of the table above that shows non-investment grade organizations are more likely to have seen their cash holdings recently shrink and, therefore, need to replenish their cash and short-term investment holdings.

A majority of organizations with non-U.S. cash and short-term investment balances intend to maintain these balances at current levels over the next year. Twenty-six percent of these organizations expect their balances of cash and short-term investments to grow over the next 12 months (an increase of five percentage points from the 2009 survey report), while only seven percent expect these balances to decrease. Two-thirds of organizations that have non-U.S. cash balances expect little change in these balances over the next year.

Expected Change in Cash and Short-term Investment Balances Over the Next Year
(Percentage Distribution)

		All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
U.S.	Larger	30%	30%	33%	29%	33%	29%	37%
	About the same	50	47	49	51	45	50	47
	Smaller	20	23	18	20	22	21	16
Non-U.S.	Larger	26%	17%	34%	14%	34%	26%	25%
	About the same	67	75	61	77	61	68	67
	Smaller	7	8	5	9	5	6	8

Investment Policies

Most organizations have a written document that defines their policies for short-term investments. Written cash investment policies outline the acceptable investment vehicles and the percentage of an organization's portfolio that may be invested in those vehicles, along with the maximum maturity allowed and the minimum credit rating necessary for each investment vehicle. Maintaining a written investment policy is considered a best practice and often is used as part of an organization's efforts to comply with regulations under Sarbanes-Oxley.

Seventy-three percent of organizations have a written document that outlines the organization's policies on cash investments. But the likelihood of organizations having such a written guideline increases significantly if those organizations are large (86 percent), are net investors (80 percent) or have investment grade ratings (82 percent). Conversely, significant percentages of smaller organizations, along with those that are net borrowers and those with non-investment grade credit ratings, do *not* have a written investment policy. Thirty-eight percent of organizations with annual revenues under \$1 billion do not have a written cash investment policy compared to 14 percent of those with annual revenues greater than \$1 billion. Two out of five net borrowers (39 percent) and 38 percent of organizations with non-investment grade ratings do not have a written cash investment policy.

Organizations with a Written Cash Investment Policy
(Percentage Distribution)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
Has a written cash investment policy	73%	62%	86%	61%	80%	82%	62%
Does not have a written cash investment policy	27	38	14	39	20	18	38

In devising their cash investment policies, most organizations strive to balance their desire for safety and liquidity with the goal of generating a competitive rate of return. Not surprisingly, safety has taken a front seat in recent years as the recession and financial crises have weighed heavily on organizations. But in what can be interpreted as a small sign of growing confidence, a small proportion of companies are now considering liquidity as their key investment objective. In 2010, three-quarters of survey respondents indicate that “safety of principal” is their organization’s key investment objective—down eight percentage points from the 2009 survey.

Twenty-two percent of survey respondents indicate that their most important cash investment policy objective was liquidity—matching the percentage reported in the 2008 survey but six percentage points higher than that in last year’s survey. But there remains a long way to go before more organizations look at their short-term investment holdings as a profit center (due primarily to the turmoil in the credit markets and the deep recession). Just two percent of survey respondents indicate that their organizations’ key short-term investment objective is yield.

Most Important Short-Term Investment Objective
(Percent Distribution of Respondents Who Have an Investment Cash Policy)

		All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
2010 Survey	Safety of Principal	76%	79%	74%	77%	77%	80%	69%
	Liquidity	22	18	25	21	21	17	31
	Return (Yield)	2	3	1	2	2	3	*
2009 Survey	Safety of principal	84%	84%	86%	84%	86%	85%	83%
	Liquidity	16	16	14	16	14	15	17
	Return (Yield)	*	*	*	*	*	*	*
2008 Survey	Safety of principal	75%	66%	80%	73%	74%	75%	70%
	Liquidity	24	28	17	23	23	23	24
	Return (Yield)	2	4	2	2	4	4	*

Organizations alter their investment policies due to a variety of factors. Those factors include changes in the financial condition of the organization, changes to the organization's risk tolerance, changes in overall market conditions (e.g., expectations for recession or economic expansion) and evolving preferences of the organization's Board of Directors or the auditors. Consequently, written investment policies are dynamic documents subject to periodic review in order to accommodate those changes.

About three-quarters (75 percent) of organizations that have written cash investment policies review and update those policies on a regular basis. Prior to last year's *AFP Liquidity Survey*, close to two-thirds of organizations with written cash investment policies reported that they updated the policies on a regular basis. The recent interest in regularly updating investment policies is undoubtedly the result of both the economic recession and the turmoil in the financial markets. Organizations that are net borrowers or those with outstanding debt that is non-investment grade are least likely to update their written cash investment policies on a regular basis.

Of those organizations that do regularly update their cash investment policies, the vast majority review those policies at least once a year. Overall, 40 percent of organizations review and/or update the policies once a year. Twelve percent of organizations with written investment policies review/update them even more frequently, some on a quarterly basis (six percent). Twenty-three percent of organizations update their cash investment policies every two to four years.

Frequency of Review/Update of Cash Investment Policy
(Percentage Distribution of Organizations with a Written Cash Investment Policy)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
Once a quarter	6%	6%	7%	3%	8%	8%	4%
Every 6 months	6	6	7	3	9	9	1
Once a year	40	40	37	30	43	43	27
Every 2-4 years	23	22	25	29	21	23	28
Not on a regular basis	25	27	24	35	19	18	40

Ninety-three percent of organizations with a cash investment policy have reviewed that policy some time over the past year, a percentage that is barely changed from that of a year ago, but an increase of 12 percentage points from the *2008 AFP Liquidity Survey*. Of the organizations that have recently reviewed their policies, just over half modified those policies as a result. Two-thirds of organizations that made alterations to their investment policy changed the relative priority placed on safety of principal, liquidity and rate of return while 42 percent have altered the list of permissible investment vehicles.

Modifications of Cash Investment Policy in Past Year
(Percent of Organizations)

Organization has neither reviewed nor modified its cash investment policy over the past year	7%
Organization has reviewed but not modified its cash investment policy over the past year	45
Relative priority placed on safety of principal, liquidity, and return	34
Permissible investment vehicles	22
Maximum maturity	10
Minimum credit rating	8
Other	3

Current Strategy

Whether or not they have a written cash investment policy, most organizations have a list of permissible investment vehicles they can hold in their short-term investment portfolio. Virtually all organizations permit the use of bank deposits as a vehicle for short-term investments. In addition, 83 percent of organizations permit the use of Treasury bills, while at least three out of five organizations allow the use of commercial paper, “pure” Treasury money market mutual funds and agency securities (62, 61 and 60 percent, respectively). In addition, 54 percent of organizations include repurchase agreements in their list of permissible investment vehicles while 53 percent do the same with “diversified” money market funds.

Less frequently permitted investment vehicles include:

- Eurodollar deposits (41 percent)
- Municipal securities (38 percent)
- Asset-backed securities (25 percent).

On average, organizations permit 4.7 investment vehicles beyond bank deposits for their short-term investment portfolio. This represents a rebound from the recent downward trend in the number of permissible vehicles since the 2006 survey. In the *2009 AFP Liquidity Survey*, the average number of permissible vehicles was 4.1.

Large organizations permit the use of an average of 5.1 investment vehicles (in addition to bank deposits and Treasury bills) for their short-term investments compared to the average 4.6 investment vehicles permitted by smaller organizations. Large organizations are more likely than smaller ones to allow the use of:

- “Pure” Treasury market mutual funds (68 percent versus 57 percent)
- Repurchase agreements (61 percent versus 46 percent)
- Eurodollar deposits (51 percent versus 31 percent).

In addition, organizations that are net investors permit a greater number of investment vehicles than do those that are net borrowers. Organizations that are net investors allow for the use of an average of 5.0 investment instruments versus 4.5 for net borrowers. An organization's credit rating appears to have little impact on the number of permissible investment holdings.

**Permissible Investment Vehicles per Organization's
Short-Term Investment Policy in Addition to Bank Deposits**
(Percent of Respondents)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade	All Responses (2009 Survey)
Treasury bills	83%	82%	84%	79%	85%	86%	78%	83%
Commercial paper	62	63	61	68	59	66	57	55
"Pure" treasury market mutual funds	61	57	68	55	67	63	61	65
Agency securities	60	60	58	55	62	61	57	56
Repurchase agreements	54	46	61	57	51	60	45	50
Diversified money market mutual funds	53	48	60	47	58	50	59	49
Eurodollar deposits	41	31	51	47	39	39	47	37
Municipal securities	38	39	35	29	43	39	31	28
Asset-backed securities	25	24	25	18	29	25	22	20
Separately managed accounts	19	17	23	11	26	21	16	16
Enhanced cash funds	16	13	18	15	17	17	16	14
Variable Rate demand notes	11	8	14	11	12	11	14	12
Auction rate securities	7	4	10	8	6	8	6	8
Mean # of investment vehicles*	4.7	4.6	5.1	4.5	5.0	4.8	4.9	4.1
Mean # of investment vehicles**	4.3	4.1	4.6	4.1	4.6	4.3	4.4	3.7

*- beyond bank deposits and treasury bills

**- beyond bank deposits and treasury bills, the count combines "pure" treasury money market funds with diversified money market funds

Cash investment policies frequently dictate the maximum proportion of an organization's cash and short-term investment balances that can be placed in specific investment vehicles. Such policies are meant to minimize risk from exposure to any single class of investment.

At least half of organizations allow at least half of their cash and short-term investment balances to be placed in Treasury bills, pure and diversified money market mutual funds, bank deposits, separately managed accounts and agency securities. Fifty-five percent of organizations limit the use of asset-backed securities to less than a quarter of their cash balances, and 49 percent limit the use of commercial paper to the same proportion of their cash balances.

**Maximum Allowable Percentage of Short-Term Portfolio That Organizations
Can Allocate to Investment Vehicle per Short-term Investment Policy**
(Percentage Distribution of Organizations Permitting Investment Vehicle)

	Up to 25% of Portfolio	25-49% of Portfolio	50% or More of Portfolio
Asset-backed securities	55%	30%	15%
Commercial paper	49	25	26
Municipal securities	47	24	29
Eurodollar deposits	44	20	36
Repurchase agreements	41	23	36
Agency securities	32	17	51
Diversified money market mutual funds	29	18	53
Bank deposits	27	15	58
Enhanced cash funds	26	35	39
Separately managed accounts	25	17	58
Treasury bills	17	8	75
"Pure" treasury market mutual funds	15	17	67

Cash investment policies also stipulate the maximum maturity length and the minimum credit quality for each type of allowable investment vehicle. For 64 percent of organizations, repurchase agreements have a maximum maturity of 90 days or less; 58 percent of organizations cap the maturity of Euro-dollar deposits also at 90 days or less. Fifty-seven percent of organizations allow separately managed accounts to have a maturity that extends beyond a year.

Maximum Maturity Allowed per Short-Term Investment Policy
(Percentage Distribution of Organizations Permitting Investment Vehicle)

	30 days or less	31-90 days	91-180 days	181-365 days	Greater than 1 year
Repurchase agreements	49%	15%	3%	26%	7%
Bank deposits	40	18	7	22	13
Diversified money market mutual funds	38	24	7	18	13
"Pure" treasury market mutual funds	32	24	4	27	13
Eurodollar deposits	29	29	6	25	10
Enhanced cash funds	22	13	13	39	13
Agency securities	15	12	6	29	38
Treasury bills	14	22	7	34	23
Commercial paper	12	25	23	34	6
Asset-backed securities	9	19	6	25	41
Municipal securities	6	15	8	27	44
Separately managed accounts	4	4	9	26	57

As was reported in previous *AFP Liquidity Surveys*, financial professionals indicate that their organizations continue to eschew risk in 2010. For most investment products, organizations have raised the minimum credit quality required for holding a particular investment vehicle. There is little relationship between organizational characteristics and the taste for lower rated investment vehicles.

Minimum Credit Quality Required per Short-Term Investment Policy
(Percentage Distribution of Organizations Permitting Investment Vehicle)

	AAA/Aaa A-1+, P-1	AA/Aa A-1+, P-1	A/A A-1, P-1	BBB/Baa A-2, P-2	Not applicable
"Pure" treasury market mutual funds	56%	9%	18%	3%	14%
Diversified money market mutual funds	54	15	21	3	7
Agency securities	53	15	17	5	10
Asset-backed securities	46	12	33	6	3
Enhanced cash funds	44	13	30	9	4
Repurchase agreements	38	20	29	4	9
Municipal securities	34	18	40	4	4
Eurodollar deposits	24	18	45	4	10
Commercial paper	23	21	41	14	1
Bank deposits	23	18	35	2	22
Separately managed accounts	22	22	26	*	30

Current Allocations

Even though business conditions have improved in 2010, businesses have remained very conservative about their short-term investment portfolio. While organizations have increased the number of investment vehicles, they are keeping two out of every five dollars of their short-term investment portfolios in bank deposits. On average, organizations invest in 2.4 types of vehicles for their cash and short-term investment balances (an increase from 1.6 in the 2009 survey but comparable to the 2.4 vehicles reported in the 2008 survey). Large organizations allocate their cash and short-term investments to an average of 2.7 vehicles compared to 2.2 for small organizations. In 2009, the averages were 2.3 and 2.2 vehicles, respectively. Net investors use an average of 2.8 vehicles compared to 2.0 vehicles for net borrowers.

Organizations allocate an average of 74 percent of their short-term investment balances in three safe and liquid investment vehicles: bank deposits, money market mutual funds and Treasury securities. While this represents a decrease from the 78 percent reported in the *2009 AFP Liquidity Survey* report, it is comparable to the 73 percent reported in the 2008 survey and an increase from the 67 percent reported in 2007. Forty-two percent of short-term investment balances are maintained in bank deposits, up by nearly five percentage points from 2009. Organizations are, however, removing money from so-called “pure” Treasury market mutual funds and Treasury bills (down 6.8 and 1.7 percentage points, respectively).

Smaller organizations place a greater percentage of their cash and short-term investments in banks than do large organizations—46 percent versus 32 percent. Large organizations are more likely than smaller ones to embrace diversified money market mutual funds (24 percent versus 11 percent). Net borrowers place nearly half of their short-term investment balances in the bank, as do organizations with non-investment grade credit ratings.

Organizations shied away from a number of investment vehicles during the recession and financial market crisis, and these vehicles continue to be used sparingly by most organizations. These vehicles include commercial paper (down 61 percent over the past two years), Eurodollar deposits, auction rate securities and variable rate demand notes. Others experienced a minor rebound over the past year; including agency securities and repurchase agreements.

Current Allocation of Organizations' Short-Term Investments
(Mean Distribution)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade	All Responses (2009 Survey)
Bank deposits	41.5%	46.3%	31.5%	49.4%	33.4%	33.6%	49.1%	37.2%
Diversified money market mutual funds	15.8	11.1	23.8	14.5	17.8	18.0	15.4	15.7
"Pure" treasury market mutual funds	9.3	9.0	10.5	6.3	12.1	7.4	12.1	16.1
Treasury bills	7.5	6.9	9.0	5.8	9.3	9.5	6.3	9.2
Agency securities	5.0	5.7	4.1	5.5	4.6	6.8	3.2	3.4
Repurchase agreements	4.6	3.6	5.6	4.9	3.8	5.1	4.3	3.5
Enhanced cash funds	2.8	3.5	1.7	2.2	3.3	2.4	2.7	1.9
Eurodollar deposits	2.7	2.0	4.1	2.8	3.0	2.9	3.4	6.0
Commercial paper	2.6	3.0	2.6	2.3	3.4	4.4	0.7	3.5
Separately managed accounts	1.8	1.9	2.0	1.1	2.7	2.4	0.9	2.1
Municipal securities	1.1	1.5	0.6	0.6	1.6	1.2	0.4	0.7
Asset-backed securities	0.7	1.2	*	*	1.4	0.9	*	0.8
Auction rate securities	0.6	*	1.2	0.9	0.2	0.9	*	0.3
Variable rate demand notes	0.1	*	0.3	*	0.2	0.2	*	0.2
Other	3.9	4.1	3.1	3.7	3.2	4.3	1.5	1.3
Mean # of vehicles	2.4	2.2	2.7	2.0	2.8	2.8	1.9	1.6
Mean # of vehicles*	2.2	2.1	2.5	1.9	2.5	2.6	1.7	1.6

* - The count combines "pure" treasury money market funds with diversified money market funds

As noted above, two out of every five dollars that organizations have in their short-term investment balances are placed in bank accounts. When investing in bank deposits, organizations use the following instruments:

- Time deposits (e.g., CDs) (63 percent of organizations)
- Non-interest bearing transaction accounts (insured through TAG) (45 percent)
- CDARS (17 percent)
- Insured cash shelter accounts (nine percent).

Time deposits are favored by organizations with annual revenues greater than \$1 billion, those that are net investors and those that hold investment grade credit ratings. Non-interest bearing transaction accounts are more widely used by smaller organizations, those that are net borrowers and those with non-investment grade ratings. CDARS are more likely to be used by organizations with investment grade ratings and those that are net investors.

Instrument Used When Investing in Bank Deposits
(Percent of Organizations That Invest in Bank Deposits)

	All Responses	Annual Revenues Under	Annual Revenues Over \$1 billion	Net Borrower \$1 billion	Net Investor	Investment Grade	Non-Investment Grade
Time deposits	63%	59%	70%	56%	68%	74%	48%
Non-interest bearing transaction accounts	45	47	40	47	40	38	53
CDARS	17	19	15	12	20	25	11
Insured Cash Shelter Accounts	9	10	7	10	7	5	13

Matching trends in previous *AFP Liquidity Surveys*, organizations place most of their short-term investment portfolio into investment vehicles that have very short maturities. On average, just under three-quarters of all short-term investment holdings are invested in vehicles with maturities of one month or less. Another 11 percent of short-term investments are held in instruments with maturities of between 31 and 90 days. Organizations that are net investors and those with investment grade credit ratings are more likely than net borrowers and those with non-investment grade ratings to hold their short-term investments in instruments with longer maturity horizons. Two-thirds of investment holdings of net investors and organizations with investment grade ratings are held in instruments with maturity horizons of less than a month, compared to more than 80 percent of holdings of net borrowers and non-investment grade rated organizations.

Most financial professionals expect their organizations to maintain the current percentage distribution of their short-term investment portfolios in terms of maturity over the next year (78 percent). Eighteen percent of organizations expect to lengthen the average maturity of their short-term investment portfolios, while four percent expect to further shorten the average maturity over the next year. In the 2009 survey, 14 percent of respondents expected their organizations would lengthen the average maturity of their short-term investment holdings while 12 percent of respondents had indicated this in the 2008 survey.

Average Maturity of Organization's Short-Term Investment Portfolio
(Percentage Distribution of Total Portfolio)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
0-30 days	74%	72%	76%	82%	67%	67%	83%
31-90 days	11	11	13	8	15	16	7
91-364 days	8	9	6	5	10	9	5
1 year or more	6	8	5	4	8	8	4
Expectations for change in average maturity of holdings over next year (Percentage Distribution)							
Lengthen	18%	21%	17%	15%	23%	23%	14%
Keep the same	78	75	80	80	74	74	83
Shorten	4	4	3	5	3	3	3

Multi-Family Trading Portals

Organizations have the option of using an electronic, multi-family trading portal to execute short-term investment transactions. These portals provide organizations an opportunity to more easily facilitate transactions and compare investment choices. In addition, trading portals can lower the costs associated with managing and administering an organization's short-term investments.

Twenty-one percent of organizations use an electronic, multi-family trading portal to execute at least a portion of their short-term investment transactions. Large organizations are more likely than smaller ones to use such a portal: 32 percent of large organizations use a multi-family trading portal compared to just 14 percent of smaller organizations. The use of multi-family trading portals has remained stable over the past few years.

Organizations' Use of Electronic, Multi-family Trading Portals to Execute Any of its Short-Term Investment Transactions
(Percentage Distribution)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
Organization uses electronic, multi-family trading portal	21%	14%	32%	19%	24%	25%	16%
Organization does not use an electronic, multi-family trading portal	79	86	68	81	76	75	84

Organizations that do use electronic multi-family trading portals use those portals to transact the majority of their money market fund transactions. Those organizations using trading portals moved an average of 73 percent of their money market mutual fund holdings through these portals, a percentage virtually unchanged from that reported in 2009. Net borrowers are the only segment that reports a higher percentage of holdings that are run through an electronic, multi-family trading portal.

Percentage of Money Market Mutual Fund Holdings That are Run Through an Electronic, Multi-Family Trading Portal

	All Responses	Annual Revenues Under	Annual Revenues Over \$1 billion	Net Borrower \$1 billion	Net Investor	Investment Grade	Non-Investment Grade
2010 Survey	73%	73%	70%	82%	64%	71%	73%
2009 Survey	72	60	79	81	66	72	69
2008 Survey	80	88	77	80	81	80	76
2007 Survey	74	87	68	75	73	71	76
2006 Survey	69	67	76	76	72	76	67

Impact of New SEC Rules on Money Market Funds

In January 2009, the Securities and Exchange Commission (SEC) voted to adopt new rules to strengthen money market funds (MMFs). The new rules focus on limiting risks associated with those funds, increasing protection of investors, improving fund operations, and enhancing fund disclosures. Responding to a tumultuous year in the money market fund world, SEC Chairman Mary Schapiro stressed that these rules changes were “just the first step” in efforts to improve money market funds’ ability to withstand market turmoil and future crises.

The amendments are designed to increase the resilience of money market funds to economic stresses, reduce the risks of runs on funds, facilitate the orderly liquidation of a money market fund that breaks, or is about to break, the buck, and improve the SEC’s oversight of money market funds.

The amendments seek these goals by:

- tightening liquidity requirements
- imposing higher credit-quality requirements
- shortening portfolio maturity limits
- addressing reliance on rating agencies
- enhancing disclosure of portfolio holdings, and
- addressing issues that arise when money market funds experience market challenges.

Some of the new rules passed by the SEC have mandatory compliance dates that were as early as May 5, 2010. Perhaps the most notable change is that MMFs are now forced to disclose if they are processing, or can process, transactions at prices other than \$1. SEC staff will collect and maintain all of this information in a newly created database that will be used for all money market funds and will be available to the public after 60 days .

Overall, financial professionals are “comfortable” with most of the specifics associated with the rule changes on MMFs. At least three out of five financial professionals are either “very comfortable” or “comfortable” with each of these specific rule changes:

- 30 percent weekly liquidity requirement
- Ten percent overnight liquidity requirement
- Decrease from ten percent to five percent of portfolio holdings for illiquid securities
- WAM from 90 days or less to 60 days or less
- Weighted average life of 120 days or less.

About half of survey respondents are “comfortable” with the 0.5 percent maximum concentration per issuer for Tier 2 and the requirement that three percent of the portfolio investment in A2/P2 paper have a 45 day limit. Only a third of survey respondents are comfortable with the 60-day lag for the release of shadow net asset values (NAV's).

Overall, respondents from large organizations and those that are net investors or have investment grade ratings are more likely to be “comfortable” the specifics of the rule changes.

Investors’ Comfort in Specific Rule Changes on MMF’s
(Percent of Respondents Who Rated Their Level of Comfort as Either a “4” or “5” Using a Five-Point Scale)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
30% weekly liquidity requirement	66%	60%	72%	58%	71%	68%	61%
10% overnight liquidity requirement	65	59	73	57	71	72	58
Decrease from 10% to 5% of portfolio holdings for illiquid securities	64	59	71	59	68	66	65
WAM from 90 days or less to 60 days or less	63	62	68	53	74	69	59
Weighted average life of 120 days or less	62	57	67	50	71	68	52
0.5% max concentration per issuer for Tier 2	51	46	58	41	60	52	51
3% of portfolio investment in A2/P2 paper with 45 day limit	48	45	53	38	57	49	47
Release of shadow NAV's on 60 day lag	35	38	31	32	38	33	37

More than two out of five survey respondents indicate that releasing the 60 day shadow net asset value (NAV) will have an impact on their organization's investment decisions related to money market funds. Twenty-seven percent of survey respondents anticipate their organization will either reduce or completely eliminate MMFs from their short-term investment portfolios because of the possibility of a NAV falling below \$1. Another 16 percent will monitor their funds closely and will sell them if/when the NAV declines under \$1. Large organizations, those that are net investors and those with investment grade ratings are more likely to indicate they anticipate dumping MMFs from their short-term investment portfolios because of the possibility of a NAV falling below \$1.

**Impact of 60-Day Shadow NAV on Organizations'
Investment Decisions in Money Market Funds**
(Percentage Distribution)

	All Responses	Annual Revenues Under \$1 billion	Annual Revenues Over \$1 billion	Net Borrower	Net Investor	Investment Grade	Non-Investment Grade
It will have no bearing	57%	65%	46%	67%	49%	50%	63%
Organization will monitor it and will sell funds that report a NAV that falls below \$1	16	10	22	15	15	13	20
Possibility of reporting NAV below \$1 would cause us to reduce MMF holdings	16	14	20	9	23	23	9
Possibility of reporting NAV below \$1 would cause us to stop investing in MMF's	11	11	12	9	13	14	8

More than two out of five respondents—including at least half of respondents from smaller organizations and those that are net borrowers—indicate that their organization is “generally comfortable” with the changes to 2a-7 funds and as a result do not expect to modify their investment strategy. Still, 30 percent of organizations anticipate diversifying their investment selections because of an expected decline in yield while a quarter of respondents report that their organization will continue to use said funds but with a reduced level of exposure.

Expected Effect of Changes on Organizations' Investment in Money Market Funds
(Percentage of Organizations)

	All Responses	Annual Revenues Under	Annual Revenues Over \$1 billion	Net Borrower \$1 billion	Net Investor	Investment Grade	Non-Investment Grade
Organization is generally comfortable with the changes and will not modify its investment strategy	45%	50%	38%	51%	40%	43%	46%
It will push yields lower overall—organization will look to diversify investment selections	30	24	38	26	34	29	35
Organization will continue to use money funds but will limit the amount of exposure to them	24	24	24	24	25	24	22
Organization seeks principal preservation yet shadow NAVs may call into question the safety of MMF's	15	8	25	9	20	18	13
Other	6	7	5	6	6	7	5
Organization will invest in non-2a-7 funds to pick up yield	5	4	5	1	7	5	5

Conclusions

Three key themes stand out from the results of *AFP Liquidity Survey*. Bank deposits are the predominant short-term investment vehicle—over 40 percent of short-term investment balances are kept in bank deposits versus only 25 percent two years earlier. This could be attributed to the FDIC-insured programs as banks were paying up to increase their capitalization over the year. There was also a shift towards liquidity versus safety as the primary driver for organizations' investment portfolios and an increased expectation towards increasing investment maturities in the coming year. This suggests a growing confidence in the markets that the worst is behind us and, therefore, companies will be looking to pickup yield again in the near-term. Nevertheless, companies remain far more conservative than they were just a few years earlier.

The effect of changes in the 2a-7 funds appears mixed during the Spring of 2010. This survey was conducted just as the changes were released into the market, with many of them being phased in at various intervals throughout the year. The major change is the effect that the 60-day shadow NAV will have on investors' appetite for money market fund headline risk. January 2011 will be the first time investors will see the shadow NAV published and the survey results indicate that a significant share of organizations will watch to see how this unfolds.

A possible offset in some of the money market fund changes could be an increase in the use of separately managed accounts as companies will look to extend maturities and capture yield over and above lower expected money market fund returns. Most of the 2a-7 rule changes will drive down yields while improving liquidity. Investors indicate they will be looking for more yield in the coming months—as a result, financial professionals expect to further examine investment alternatives as business conditions improve.

Bank deposits remain a safe and liquid place in which to invest and as the economic conditions improve, it will be interesting to see when corporate investors shift from investment vehicles that are safe and liquid to those that may offer higher yield. With the added transparency in 2a-7 money funds, those organizations that have a written investment policy will want to make sure their money fund investments fit within their organizations' current guidelines or at least review them in light of the proposed changes.

About the Survey

In May 2010, the Association for Financial Professionals conducted a 27-question survey on strategies associated with the management of short-term investments. AFP received 276 responses from its corporate practitioner members. After adjusting for mis-delivered email, the response rate was approximately ten percent. An additional 61 responses were received from corporate practitioners who are not AFP members. The combined 337 responses are the basis of this report. The survey was underwritten by Promontory Interfinancial Network, LLC. The survey questionnaire and report were produced by the Research Department of the Association for Financial Professionals, which is solely responsible for the content of the report.

The demographic profile of the survey respondents mirrors that of AFP's membership. The following table summarizes the characteristics of the survey respondents.

Industry Classification (Percentage Distribution)

Manufacturing	17%
Retail (including wholesale/distribution)	14
Financial services	10
Insurance	8
Energy (including utilities)	7
Health services	7
Business services/Consulting	6
Non-profit (including education)	6
Telecommunications/Media	6
Government	5
Software/Technology	4
Transportation	4
Construction	2
Hospitality/Travel	2
Real estate	2

Annual Revenues
(Percentage Distribution)

Under \$50 million	17%
\$50-99.9 million	4
\$100-249.9 million	8
\$250-499.9 million	13
\$500-999.9 million	15
\$1-4.9 billion	31
\$5-9.9 billion	5
\$10-20 billion	3
Over \$20 billion	4

Ownership Type
(Percent Distribution)

Publicly owned	38%
Privately held	43
Non-profit (not-for-profit)	10
Government (or government-owned entity)	8

Net Borrower or Net Investor
(Percentage Distribution)

Net Investor	44%
Net borrower	56

Organization's Credit Ratings
(Percentage Distribution)

Investment grade	61%
Non-investment grade	39

AFP Research

AFP Research provides financial professionals with proprietary and timely research that drives business performance. The AFP Research team is led by Managing Director, Research and Strategic Analysis, Kevin A. Roth, PhD, who is joined by four research analysts. AFP Research also draws on the knowledge of the Association's members and its subject matter experts in areas that include bank relationship management, risk management, payments, and financial accounting and reporting. AFP Research also produces *AFP Econ Watch*, a weekly economic newsletter. Study reports on a variety of topics, including AFP's annual compensation survey, and *AFP Econ Watch*, are available online at www.AFPonline.org/research.



About the Association for Financial Professionals

The Association for Financial Professionals (AFP) headquartered in Bethesda, Maryland, supports more than 16,000 individual members from a wide range of industries throughout all stages of their careers in various aspects of treasury and financial management. AFP is the preferred resource for financial professionals for continuing education, financial tools and publications, career development, certifications, research, representation to legislators and regulators, and the development of industry standards.

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