

Basel III Reshapes Banks' Relationships with Corporate Treasury

New regulations could disrupt companies use of bank deposits just as SEC regulatory changes threaten to make money funds less attractive.

By Susan Kelly | Updated on May 21, 2014

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More than five years after the financial crisis, reforms designed to make the financial system safer are filtering down to the world of corporate treasury. Basel III capital standards are starting to affect companies' relationships with their banks, while the prospect of changes in the regulations governing money-market funds has created uncertainty around short-term investing.

"The front end of several years' worth of the regulatory hammer is flowing through the banks and reaching the treasurer's desk," said Anthony Carfang, a partner at consultancy Treasury Strategies.

He pointed out that as national regulations implementing the Basel III standards are phased in beginning next year, two parts of the standards will have particular relevance for treasuries: the leverage ratio and the liquidity coverage ratio.


The leverage ratio limits how big a bank's balance sheet can be, which means banks may have less interest in making loans. That's why "a treasurer's got to make sure that the company's borrowing resources are diversified and they're not simply reliant on banks for short- and intermediate-term funding," Carfang said. He added that the leverage ratio "probably also increases the cost of borrowing, but slightly."

JPMorgan chairman and CEO Jamie Dimon said last month in his annual letter to shareholders that the cost of committed but unused credit revolvers could increase as much as 60 basis points as a result of new regulations that "impose liquidity and additional capital requirements" on such revolvers.

The liquidity coverage ratio is expected to have an even greater effect on treasurers' dealings with their banks. The ratio, which measures whether banks are prepared to handle cash outflows over a 30-day stress period,

operating deposits “reflect a deep relationship with the customer,” Carfang said. “A non-operating deposit is considered to be extra money that the banks probably had to go out and pay a rate in order to attract, or money customers have on deposit that could leave quickly and therefore is less a source of liquidity for the bank.” He noted, though, that regulators have yet to provide “hard and fast definitions” of the two types of deposits.

Basel III standards make non-operating deposits much less attractive to banks; they will have to back them with high-quality liquid assets, such as government bonds.


 Elizabeth Minick of Bank of America Merrill Lynch The liquidity coverage ratio will determine how financial institutions value the deposits of their corporate customers, said Elizabeth Minick, head of U.S. corporate treasury sales for Bank of America Merrill Lynch Global Transaction Services. “That’s the whole crux of the conversation.”

Whether a company’s deposits are deemed operating or non-operating will correlate to a large extent with the depth of the relationship between the bank and the company, said Minick, pictured at left.

“If you have a deep, broad treasury management relationship with a specific client, then the majority of those balances stand a good chance of being deemed operating,” she said. “If your relationship is just holding deposits, those balances are more likely to be defined as non-operating.”

Minick suggested that “at the most rudimentary level,” a bank that has a company’s accounts payable and accounts receivable business would likely be able to consider most or all of the balances in the accounts used for that business to be operating balances.

Cindy Gerhard, the managing director responsible for global product management for liquidity management services at Citi, said the Basel III regulation requires banks to assess the volume of a company’s operating business relative to the amount of money on deposit to determine the amount attributable to supporting the operating services and any excess cash buffer.

“The greater the difference  Cindy Gerhard of Citi between the operating flows and the average balance, the more likely that some of the balance will be classified as non-operating,” said Gerhard, pictured at right.

Citi is preparing to roll out a new product, a 31-day-

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notice account, which produces deposits that line up with

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"It's a time deposit with a minimum maturity of 31 days,"

Grinstead said. If the client wants to withdraw some of the money in the account, they let the bank know, and "31 days later the money will settle into their account," she said.

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Citi also plans to offer its earnings credit rate product outside the United States, starting in coming months with Western European branches, in the expectation that clients will have an incentive to grow their operating business with Citi by using the value of their deposits to offset fees.

Pushing for More Treasury Business

Banks have always pushed for more business from their corporate customers, Carfang said, but under the new rules, gaining additional corporate business "goes from a relationship enhancer to a requirement."

If a company has money on deposit but doesn't do the kind of business with the bank that would qualify those funds as operating deposits, the bank might discourage the company from depositing money, or only accept the deposit if the company agrees to leave it in the bank for a certain period of time, he said.

Minick said that as client relationships involving only deposits become less attractive for banks going forward, banks may be likely to steer customers and their funds away from deposits, which reside on the bank's balance sheet, to non-balance-sheet products such as money-market accounts.

The Basel III changes come at a time when U.S. corporations are holding considerable amounts of cash, and Thomas Hunt, director of treasury services at the Association for Financial Professionals, noted that much of that corporate cash is in bank deposits or bank products. With short-term interest rates so low, the earnings credit rate has looked attractive to companies, he said, and treasurers are comfortable with their counterparty credit risk with their banks. But given the Basel III changes, companies may need to think about alternative places to put their cash, which could be somewhat longer-term bank products, money-market funds, or government securities, Hunt said.

Of course, there's also uncertainty surrounding money-market funds at this point given the Securities and Exchange Commission's proposed regulatory changes. The SEC has suggested that money-market funds switch from using a stable net asset value (NAV) to a floating

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But a floating NAV would pose a problem for treasury departments which would have to track the fluctuations in NAV as short-term capital gains and losses for tax purposes, something their systems currently aren't set up to do.

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Depending on what changes the SEC implements, "money funds become somewhere from slightly less attractive to a lot less attractive than they are today," Carfang said. "A company treasurer whose investment portfolio is built around money funds ought to seriously be thinking about other things the company should be doing with its cash."

Minick said that treasurers should consider updating their investment policies to be sure that they're prepared if they have to make changes. "They may need to expand the number of banks with whom they place deposits, they may need to allow for non-balance-sheet items to place deposits," she said.

"It's a very interesting combination of events," Minick said. "You have pending [Basel III], possible money-market mutual fund reform, and you tie those two with the fact that our clients are holding larger cash balances than they have in history. It makes for a very interesting time."

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