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More than Meets the Eye

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To the uninitiated, managing cash might seem a simple task. After all, how difficult can it be to determine how much you have to invest, to pick an instrument that provides acceptable liquidity and a fair return, to execute the buy and when the investment matures, to repeat the process?

Active cash management, however, is a vastly more complex undertaking comprised of sophisticated analysis that requires a special blend of insight, understanding and expertise.

Before every investment decision, we examine a wide variety of factors to help guide our judgments. Among those we look at:

- ▶ Duration management. This analysis is based upon the Federal Reserve's short-term rate bias, the U.S. Treasury yield curve and the availability of the different classes of fixed income securities, with a view toward maintaining each client's overnight liquidity requirements while obtaining the portfolio's need for longer-term returns.
- ▶ GAP analysis. This method enables us to take into consideration future interest rate projections to help determine breakeven points. To illustrate: using GAP analysis, we can assess whether it's more attractive to buy a 6-month bond now – and another 6-month bond in February 2010 – versus buying a 1-year security today.
- ▶ Option-adjusted spread analysis. In contrast to the simple yield curve spread analysis that measures a bond premium over a pre-determined cash flow model, this methodology describes the market premium over a model that includes two types of volatility: variable interest rates and variable prepayment rates. This technique enables us to evaluate the attractiveness of callable bonds vs. bullets (non-callable bonds), and to help determine whether we're being fairly compensated for the optionality of the callable bond.
- ▶ Sector rotation. In concert with our Credit Analyst, the Portfolio Management team performs this ongoing analysis to identify relative value between different sectors within the fixed income universe.

The recent addition of Supranationals to our approved list of short term investment alternatives is a good illustration of "Sector Rotation". Supranationals are institutions that have been established and are controlled by a collection of governments empowered to promote economic development. The World Bank (IBRD) is the largest and most recognizable Supranational organization. Historically, Supranationals were known for issuing longer dated debt, and any short debt outstanding did not offer attractive yields relative to U.S. Agency and TLGP (Temporary Loan Guarantee Program) securities. Due to increased funding needs worldwide, however, Supranationals have recently issued several 2-year securities which not only offer yield pickup versus Agencies and TLGP paper, but also provide asset class diversification.

At Horizon we utilize all tools and analysis available to find investments that provide attractive yield enhancement while maintaining our commitment to capital preservation.

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