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An Increasing Appetite for Money Market Sweeps

■ BY STEVE GARMHAUSEN

Reserve Management Corp., the New York company that created the first money market fund, says it is gathering assets quickly, in part because its funds' reputation for safety is well received during volatile periods in the equity markets.

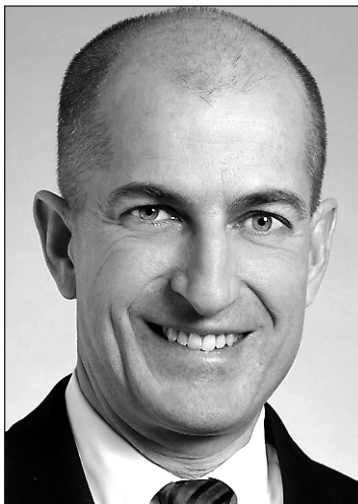
But another reason is that banks are increasingly using the company's money market sweep accounts in arrangements that allow them to compete for more commercial deposits, according to one of the Reserve Management's top executives.

By the end of February, Reserve Management had nearly doubled its assets under management from a year earlier, to more than \$100 billion.

The money market industry's overall assets increased 42% over that period, to more than \$3.4 trillion, an industry record, according to the Investment Company Institute.

"A lot of it is that our conservative nature is more appreciated during volatile times," said Bruce Bent 2nd, the president and vice chairman of Reserve Management, and his company, which uses the brand The Reserve, has had very little exposure to subprime mortgage debt.

Its 350 banking customers generate a large portion of its business, and their adoption of the firm's cash sweep product has been one key to its asset



Reinhard: Most new National Penn commercial clients use the account.

growth, he said during an interview last week.

National Penn Bancshares Inc. of Boyertown, Pa., typifies the banking companies that are using sweeps in place of repurchase agreements, according to Mr. Bent.

Michael Reinhard, National Penn's chief financial officer and treasurer, said it started working to move commercial customers from such agreements into sweep accounts two years ago.

Banks are not allowed to pay interest for corporate checking accounts, so they offer repurchase agreements as a way to earn interest on deposits that would otherwise be idle.

The customer uses its cash at the end of the day to buy investment securities from the bank, which buys them back the next morning.

"The problem is that we have become limited in the amount of securities we can use for these repos," Mr. Reinhard said in an interview last week. "We have more commercial deposits than we have securities to repurchase."

That put National Penn at a disadvantage as it competed for funding from corporations, municipalities, and other big depositors that insisted on being paid interest

To resolve the situation, the banking company started using Reserve Management's money market sweep account, which lets corporate deposits accrue interest legally while freeing up National Penn's securities.

However, there is another obstacle: Regulations allow such transactions only a few times a month unless they are done at the teller window.

To overcome that obstacle, Reserve Management personnel began to work in National Penn branches to perform the transactions face to face, according to Mr. Reinhard.

The shift to sweep accounts helped his company increase its deposits 3.3% last year, to \$3.95 billion at yearend.

Chris Nichols, the president and chief

executive officer of Banc Investment Group LLC, a San Francisco capital markets subsidiary of Pacific Coast Bankers' Bancshares, said that with corporate cash flowing into the safe harbor of banks, many companies have found themselves in situations like National Penn's.

"More money has flowed in there than expected, so banks are hitting the limit on the securities they have to pledge, and they are in a bind," Mr. Nichols said.

As a result, over the last six months

many bankers have turned to money market sweep products.

In January, Banc Investment Group began offering community banks a sweep account that let them customize interest rates as they compete for commercial checking accounts. That product is built on technology that was developed by Reserve Management, according to Banc Investment Group.

Mr. Reinhard said that the percentage of National Penn commercial customers using the money market sweep account has not

yet reached 50%, though most of its new customers are signing up for the account.

Some corporate customers insist on using repurchase agreements instead, because they want collateral for their deposits in the form of investment securities, he said; for that peace of mind, they are willing to settle for an interest rate slightly lower one they could get for the money market funds.

Mr. Garmhausen is a regular contributor to American Banker.

To learn more about The Reserve Cash SweepSM

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