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Companies Show Little Interest in Interest

U.S. companies have billions in their checking accounts, but most will forego the chance to earn interest on those balances in order to keep government guarantees on their money in place.

Companies can start earning interest on new accounts banks are rolling out with the July 21 expiry of Regulation Q, a Depression-era ban on interest-bearing corporate checking accounts. But with that opportunity comes risk most companies apparently aren't willing to bear: giving up a blanket guarantee on their money from the Federal Deposit Insurance Corporation. Low interest rates makes the trade off particularly unappealing.

"Return of capital is far more important today than return on capital," said Terry Crawford, treasurer of AMC Theatres, which operates movie theatres across the United States.

Phil Lindow, head of liquidity in JP Morgan's treasury and securities services group, said he didn't expect many companies to leap at the chance to get into interest bearing accounts, given general economic uncertainty.

The decision to leave money on the table highlights how risk averse U.S. companies remain years after the worst of the financial crisis – and well into a period of record profitability.

The new checking account options also bring attention to a little known corner of the corporate cash management world. In lieu of the interest they were banned from paying under Regulation Q, over the years banks have developed so-called earnings credit rate accounts. These pay credits based on the size of deposits that can be used to reduce the transaction fees that banks normally charge for basic services such as wire transfers or check processing.

"It's like investing in Treasurys," Crawford said of the ECR accounts. "But the rate is more attractive, and it's very safe."

Such accounts currently offer corporations anywhere between 0.20% and 0.65% in credits based on the size of their deposits, depending on the account and the institution. Crawford said that he's seen rates between 0.30% and 0.65% at the banks he deals with. While low, the rates are still much higher than the 0.03% yield of three-month Treasuries, or the 0.13% company would earn by investing in three-month commercial paper.

Making the accounts more attractive: the FDIC offers a 100% guarantee on all deposits in non-interest bearing accounts. The guarantee was first offered under the agency's temporary liquidity guarantee program in November 2008 to protect banks who were worried that companies would begin pulling money out of their accounts. First slated to expire at the beginning of 2010, protection was extended by the Dodd-Frank financial system reform act to Dec. 31, 2012.

Brad Larson, global treasurer of jewelry retailer Claire's Stores, said that ECR accounts have become more attractive to him since the FDIC adopted its guarantee, and because of the lack of viable investment options that offer both interest and safety.

"In the past, you were getting 5% or 6% investing in short-term treasuries, as opposed to 30 or 20 basis points on an earnings credit," he said, noting that getting anything approaching that higher return today entails taking on more risk, which is not in the company's interest. "Companies are afraid."

Companies had about $543 billion in ECR checking accounts as of October 2010, according to consulting firm

Treasury Strategies Inc.

The accounts are an important source of core deposits for the banks, which also see them as a way to strengthen relationships with businesses. Being at the center of companies' cash management efforts allows banks the chance to provide more lucrative services, including M&A and capital markets advice.

Michael Berkovitz, a managing director in Citi's global transactions services unit, said the FDIC's guarantee has been the chief reason more companies have been using the ECR accounts to house their cash. He said the accounts also make cash management easier, in that treasurers no longer have to constantly monitor various short-term investments in order to maximize yield, as well as limiting the number of counterparties they deal with.

"They don't have to do anything but leave it in the ECRs," he said.

But the repeal of Regulation Q changes things. Bank of America issued a white paper in February that outlined options for new accounts, including sweep accounts that take any excess money in the ECRs and put it in interest-bearing accounts in the U.S., as opposed to offshore accounts. Another option includes hybrid accounts that pay both earnings credits and hard-dollar interest.

For AMC's Crawford, however, the FDIC's guarantee trumps any consideration. He said that as long as the 100% guarantee is in place, he'll be hard pressed to take his money out of the ECRs.

"If [the guarantee] doesn't get extended again, we'll probably see a shift," he said.