

Exploring the world of Cash funds

With the fallout surrounding Northern Rock, Bradford & Bingley and the collapse of the Icelandic banking sector it is not surprising that cash deposits in banks and building societies have become a hot topic.

Before the government rescue of Northern Rock most people had never heard of the Financial Services Compensation Scheme, let alone know what level of protection it provided. It was assumed that if your money was placed with a high street bank it must be safe.

The recent uncertainty surrounding the protection of cash deposits in UK banks and building societies has resulted in an increase in questions from investors about cash funds. The purpose of this fact sheet is to provide greater clarity as to what cash funds are, how they might be used and what the Friends Provident Cash Fund actually invests in.

What are Cash funds?

- Cash funds, also known as Money Market funds, invest in the Money Markets. The Money Markets are financial markets in which money is borrowed or loaned for short periods, usually for a period of less than one year.
- The funds invest in a range of financial instruments, such as Certificates of Deposit (CD). CDs are negotiable certificates, representing a bank's obligation to repay money deposited with it, earning specified rates of interest over a given period of time.
- In comparison with share and fixed interest based funds, cash funds have historically been categorised as lower risk investment funds.

Are Cash funds similar to bank accounts?

- No, unlike bank accounts cash funds are managed by investment professionals that pool together the money from thousands of investors, and then invest it in a range of financial instruments, such as Certificates of Deposit.
- In addition to this, when the Bank of England changes its base rate, some banks may take the decision to immediately alter the rates of interest available through their accounts. However, there would be no immediate direct effect upon a cash fund. The base rate change would feed through when the existing cash fund holdings mature and are replaced by new ones based on the revised base rate.



Why invest in a Cash fund?

- An investor might use a cash fund as a temporary home for their money before deciding which other funds they want to invest in. However, they are not a particularly suitable investment for the majority of investors over the long-term as the value of an investment in cash could be eroded over time due to the effects of inflation.
- A cash fund could be combined with share and fixed interest based funds to help balance a pension portfolio.
- For more active investors it could act as a temporary haven during periods of stock market volatility.
- As pension investors near their retirement date, to provide some protection against stock market volatility, some investors might decide to invest part of their portfolio into a lower risk rated fund, such as a cash fund, to protect the value of their fund.

What does the Friends Provident Cash Fund invest in?

- The Friends Provident Cash Fund predominantly invests in very short-dated financial instruments, such as Certificates of Deposit, with less than three months until they mature.
- Exposure to any single issuer of financial instruments is limited to a maximum of 5% of the Fund's portfolio.
- Just like an investor might have his own credit assessment so do banks. F&C Asset Management, who manage the Friends Provident Cash Fund, have an internal credit committee that carries out credit assessments and sets limits for individual bank exposures. If there were concerns about a bank the limits would either be reduced or F&C would stop investing in them.
- In the current environment preference is being shown towards banks that have the backing of their national government.

What rate of return can I expect from the Friends Provident Cash Fund?

- The Fund is not like a bank account that offers a variable or fixed rate of return. The Friends Provident Cash fund is managed by a team of investment professionals that pool together the money from thousands of investors, and then invest it in a range of financial instruments.
- How much an investor gets back is dependent upon how well the Fund's investments perform. An investor may see the value of their investment go up and down in value.

In light of the current financial crisis, are there any plans to make any significant changes to what the Friends Provident Cash Fund can invest in?

- The Fund will continue to invest in very short-dated financial instruments, such as Certificates of Deposit, with less than three months until they mature.
- In the current environment preference is being shown towards banks that have the backing of their national government.

Key Points

- Cash funds pool together the money from thousands of investors and then invest it in a range of financial instruments.
- The Friends Provident Cash Fund predominantly invests in very short-dated financial instruments, such as Certificates of Deposit, with less than three months until they mature.
- The Friends Provident Cash Fund is currently favouring banks that have the backing of their national government.
- How much an investor gets back is dependent upon how well the Fund's investments perform. The value of an investment is not guaranteed and an investor could get back less than they've paid in.
- Any investor needing advice on their pension or investments should speak to their financial adviser. Anyone without a financial adviser can find one in their area at www.unbiased.co.uk.

