PART 6

MANAGING COUNTERPARTY RISK IN CORPORATE CASH PORTFOLIOS

A Strategic Framework for CFOs and Treasury Teams

CAPITAL ADVISORS GROUP

Managing Counterparty Risk in Corporate Cash Portfolios

In an era defined by financial complexity, banking concentration, and episodic market shocks, risk management is a core responsibility for corporate treasury teams.

For institutional cash investors, effective cash management may go beyond preserving capital. It may be supported by a proactive, forward-looking approach built on three disciplines:

- Integrated counterparty risk management
- Credit insight
- Portfolio-level diversification

An effective framework can help bring these elements together—providing a timely view of exposures across the enterprise. This may allow treasury teams to make informed decisions and respond quickly as market conditions change.

How Risk in Corporate Cash Management is Evolving

Traditionally, corporate treasury risk management largely focused on:

1.



PRESERVING PRINCIPAL

2.



MAINTAINING LIQUIDITY THROUGH BANK DEPOSITS AND MONEY MARKET FUNDS

Today, institutional investors have access to a wider array of investment options that may be used to address liquidity, risk, and yield objectives—expanding both opportunity and complexity.

At the same time, structural changes in the financial system have created new challenges for managing risk, including:



BANKING SECTOR CONCENTRATION

In many markets, fewer institutions now hold a larger share of global deposits and assets



GREATER FINANCIAL COMPLEXITY

Investment products and counterparty exposures may involve more layered and interconnected structures



REDUCED EXPECTATIONS OF GOVERNMENT SUPPORT

Regulatory reforms have sought to reduce tax payer funded support, making bailouts less certain in the event of institutional failure



GLOBAL CONTAGION RISK

Increased financial interconnectedness may increase the potential for shocks to spread more quickly across markets

As a result, counterparty risk—the risk that a financial institution fails to fulfill its obligations—has become increasingly for corporate treasury teams. Managing this risk effectively may help support liquidity objectives, capital preservation, and operational stability.

Building an Integrated Risk Management Framework

In this environment, effective risk management is supported by a systematic, not reactive approach.

Capital Advisors Group recommends a “capture–analyze–manage” framework to help institutional treasury teams better understand and control risk across the organization:

CAPTURE

Identify and consolidate all exposures across banking partners, issuers, and investment portfolios

ANALYZE

Standardize data and assess risk using consistent credit metrics and evaluation methods

MANAGE

Actively adjust and rebalance exposures to stay aligned with defined risk tolerance and policy limits

This framework reflects an important reality: risk is not static. It evolves with market conditions, counterparty credit quality, and portfolio composition.

For that reason, treasury teams may benefit from an ongoing process of monitoring and adjustment—rather than simply relying on static policies.

For a deeper look at implementation, explore the "capture-analyze-manage" approach to institutional risk oversight.

Understanding Counterparty Risk Beyond Default

Among all risk categories, counterparty risk is often a critical consideration for corporate cash investors.

Confidence in financial institutions can rapidly erode—driven by bank runs, rapid deposit outflows, or forced mergers.

But, counterparty risk extends beyond outright default, and may include:

- Delayed payments
- Liquidity constraints
- Legal disputes or operational failures

As a result, effective risk management often involves evaluating both a counterparty's ability and willingness to meet its obligations.

Diversification: The First Line of Defense

Diversification is the foundation of effective counterparty risk management.

However, true diversification goes beyond simply spreading deposits across multiple banks.

KEY DIMENSIONS OF DIVERSIFICATION

- **Issuer diversification** – Limit exposure to any single counterparty
- **Sector diversification** – Reduce concentration across sectors by expanding into other high-quality issuers
- **Investment diversification** – Incorporate a mix of instruments, including direct investments of short-term assets

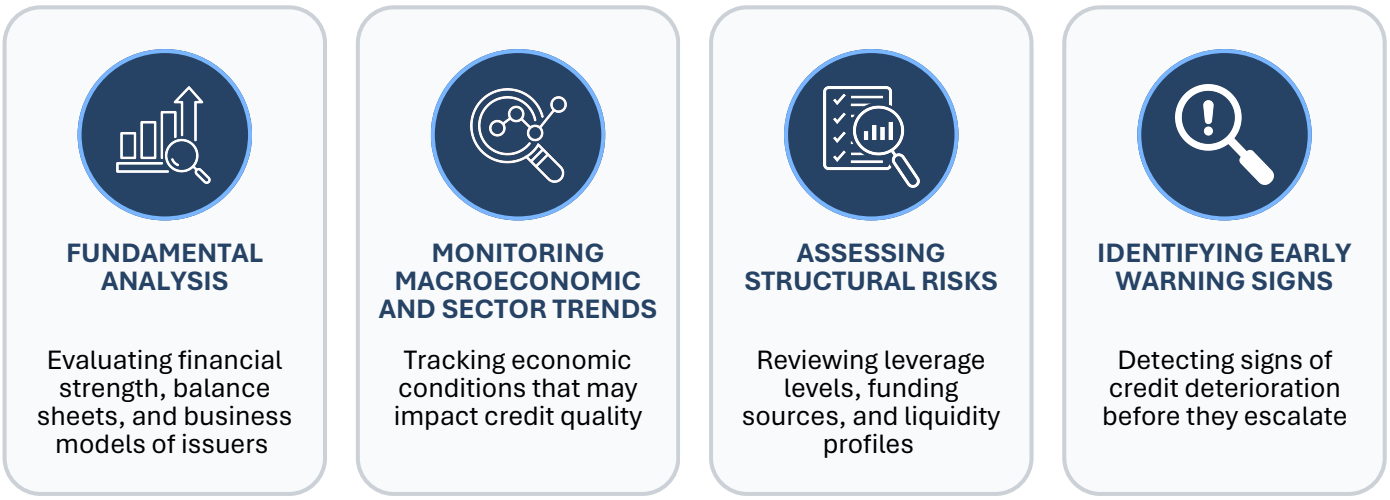
Directly owned securities—like those held in a separately managed account—may help offset concentrated bank exposure.

For example, a treasury portfolio heavily weighted toward bank deposits may reduce overall risk by allocating a portion to Treasury, Government Agency, Commercial Paper, high-quality corporate or asset-backed securities.

By diversifying across issuers, sectors, and instruments, treasury teams may benefit from more resilient cash portfolios that are well positioned to withstand market stress.

The Role of Credit Insight in Risk Management

Diversification alone may not be sufficient and may be more effective paired with ongoing credit analysis.



This level of analysis is important because financial institutions may be unpredictable and may be influenced by leverage, opaque exposures, and confidence-sensitive funding.

By combining diversification with deep credit insight, treasury teams may be positioned to a more proactive approach to managing counterparty risk and protecting capital.

Managing Cash Portfolios in an Uncertain Macro Environment



Corporate cash investors must also navigate a range of macroeconomic risks including:

- Interest rate volatility
- Inflation uncertainty
- Geopolitical events
- Regulatory changes



To manage these risks effectively, treasury teams may benefit from adopting an active portfolio management approach, which may include:

- Modifying portfolio duration to manage interest rate exposure
- Reallocating across sectors to reduce concentration risk
- Selecting high-quality securities based on current market conditions

In periods of uncertainty, this adaptability can be beneficial—enabling treasury teams to respond dynamically rather than relying on static investment strategies.

Best Practices for Institutional Risk Management

A strong risk management strategy often includes clear structure, defined limits, and continuous oversight.

The following best practices may help treasury teams build a more resilient framework:



ESTABLISH A COMPREHENSIVE RISK POLICY

Develop an umbrella policy that governs all exposures—including bank deposits, investments, and derivatives—under a unified framework.



DEFINE CLEAR RISK LIMITS

Set explicit guidelines for issuer exposure, minimum credit quality, and maturity thresholds to prevent unintended concentration.



INTEGRATE CREDIT RESEARCH

Leverage internal or external credit expertise to support investment decisions and ongoing risk monitoring.



USE SCENARIO ANALYSIS

Conduct “what-if” scenarios to help understand how changes in market conditions or counterparty health could impact the portfolio performance and liquidity.



CONTINUOUSLY MONITOR AND REBALANCE

Treat risk management as an ongoing process by regularly reviewing exposures and adjusting allocations as market conditions evolve.

Separately Managed Accounts (SMAs) for Cash Risk Control

A separately managed account (SMA) is a tool used for managing liquidity and risk in corporate cash portfolios.

Unlike pooled investment vehicles—such as money market funds—SMAs provide direct ownership and control of individual securities, supporting more precise risk management.

KEY ADVANTAGES OF SMAs



1.

FULL TRANSPARENCY AND CONTROL

SMAs provide treasury teams with transparency into directly owned holdings in the portfolio.

Key benefits include:

- Monitoring of issuer exposure
- Customization of credit criteria and maturity limits

Ability to evaluate and respond to deteriorating credit conditions in a timely manner. With SMAs, risk is managed at the individual issuer level, rather than at the fund level—supporting more precise decision-making.



2.

CUSTOMIZATION ALIGNED TO RISK POLICY

SMAs are built around an Investment Policy Statement (IPS), designed to reflect your organization's specific needs.

This typically includes:

- Approved security types
- Minimum credit quality standards
- Duration and maturity limits
- Issuer concentration thresholds

This approach may provide greater flexibility in aligning your cash portfolio with liquidity needs, risk tolerance, and investment objectives—rather than adapting to a one-size-fits-all product.



3.

ACTIVE PORTFOLIO MANAGEMENT

SMAs are actively managed portfolios, which may provide flexibility for treasury teams to adjust quickly as market conditions change.

This may include:

- Reducing exposure to higher-risk counterparties
- Increasing allocation to high-quality or diversified assets
- Adjusting duration to manage interest rate risk

This flexibility may be beneficial during periods of market volatility, when risks can shift rapidly.

Explore how SMAs can support institutional cash and liquidity strategies.

Technology as a Force Multiplier in Risk Management

Technology is transforming how treasury teams manage counterparty risk—often providing greater visibility, faster insights, and more informed decision-making.

Platforms like CounterpartyIQ®, developed by Capital Advisors Group, illustrate how technology can support modern cash management strategies.

CounterpartyIQ® analyzes more than 100 characteristics for each issuer, combining quantitative metrics with qualitative analysis to produce a comprehensive view of credit risk.



KEY CAPABILITIES INCLUDE:

- **Continuous credit monitoring of counterparty credit profiles**
- **Enterprise-level risk aggregation of exposures across counterparty relationships**
- **Actionable risk controls delivering alerts when custom risk tolerance thresholds have been breeched**
- **Portfolio construction support with approved buy lists aligned with established credit standards**
- **Enhanced governance and transparency with continuous oversight and monitoring of risk exposures**

By leveraging technology-driven insights, treasury teams can move from solely manual monitoring to proactive, data-driven risk management.

This added layer of intelligence may assist treasury teams in decision making and risk oversight as they manage their corporate cash portfolios.

The Bottom Line: From Passive Risk Oversight to Active Risk Management

The role of corporate treasury has evolved. Today, it extends beyond serving as a steward of liquidity to include actively managing risk in a complex and rapidly changing financial environment.

By combining a structured risk framework with rigorous credit analysis, treasury teams may be better positioned to:



Gain a clearer view of exposures across the organization



Support more informed, data-driven decisions



Respond to changing market changes in a timely manner

Importantly, the goal is not to eliminate risk—but to understand, measure, and manage it deliberately.

In doing so, risk may become more than a challenge. It may serve as a strategic tool—helping organizations strengthen resilience and support their cash investment strategy.



Key Insight for CFOs and Treasury Leaders

Counterparty risk is no longer a static credit concern—it's a dynamic portfolio management challenge that should be measured, diversified, and actively managed across all exposures.



Next Step For Finance Teams

Evaluating your current cash and banking relationships through a counterparty risk lens—assessing concentration, credit exposure, and visibility—and determine whether your framework allows for real-time monitoring and proactive risk rebalancing.

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Capital Advisors Group, Inc. is an independent SEC-registered investment advisor specializing in institutional cash investments, risk management, and debt finance consulting. Our clients range from venture capital-funded startups and emerging growth companies to Fortune 100 companies.

Drawing upon more than a quarter of a century of experience through varied interest rate cycles, the firm has built its reputation upon deep, research-driven investment strategies and solutions for its clientele.

Capital Advisors Group manages customized separately managed accounts (SMAs) that seek to protect principal and maximize risk-adjusted returns within the context of each client's investment guidelines and specific liquidity needs. Capital Advisors Group also provides FundIQ® money market fund research; CounterpartyIQ® aggregation and credit analysis of counterparty exposures; risk assessment on short-term fixed income securities and portfolios; and independent debt finance consulting services.

Headquartered in metropolitan Boston, Capital Advisors Group maintains multiple U.S. regional offices.

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CAPITAL
ADVISORS GROUP

Capital Advisors Group, Inc.
One Federal Street, Suite 2200
Boston, MA 02110
Tel: 617.630.8100 ~ Fax: 617.630.0023
www.capitaladvisors.com
info@capitaladvisors.com