

# Money Fund Report®

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LEADING THE INDUSTRY IN MONEY FUND NEWS

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## ◆ TREASURY-ONLY MMFs EQUIVALENT TO T-BILLS, SAYS REPORT

Treasury-only money-market funds are the “functional equivalent” of Treasury bills and should be treated as such for purposes of collateral management. That is what is recommended in a recently-published paper, “Collateral Scarcity: An Approach to Preventing Market Stress from Becoming Contagion.”

Written by corporate treasury consulting firm Treasury Strategies, the paper makes its case by describing several situations and scenarios “that may prevent collateral from being readily available” and, noted the accompanying release, “There is compelling evidence to conclude that collateral scarcity may arise during market stress.”

Driving the paper is the post-crisis landscape where dramatic increases in collateral requirements have accelerated growth in the demand for high-quality assets that has far outstripped the growth of supply. The paper cited a Treasury Borrowing Advisory Committee estimate that the requirement to centrally-clear derivatives alone will “increase global demand for OTC trading-related collateral to \$0.8- \$2.0 trillion in normal market conditions, and \$1.8-\$4.6 trillion in a stress scenario.”

Tony Carfang, director at Treasury Strategies, spoke with *Money Fund Report*® and touched on several points underscoring the need for this proposal to be taken seriously.

Carfang discussed accessibility to the market as he made his argument for the use of Treasury-only money-market funds as collateral. He explained, “The biggest institutions are also the biggest players in the plumbing of the financial system so they have good access to collateral. The next level down, including corporate treasurers, smaller institutional investors and municipalities, are usually buying their securities not from the Treasury itself but from the dealer. If there’s a shortage of collateral and the dealer needs some and the dealer’s customers need some, who is the dealer going to give it to? The dealer is going to keep it.” Those who are unable to procure the needed collateral, he stated, will have to “exit the market.”

Other reasons for a collateral shortage include long-term holders of high-quality assets that would otherwise qualify as collateral. “The Treasury bill in my mother’s vault isn’t going to be used as collateral because it’s in my mother’s vault. The Treasury bills that are held in China are going to stay in China,” said Carfang.

What the paper described as “operational bottlenecks” are concerning. Carfang explained, “If you are a bank, you cannot afford to violate one of your Basel III requirements. The markets are in stress and you think there’s going to be a shortage of collateral – of Treasuries. Do you hold just enough to meet today’s requirement or do you get an extra 10 or 20 percent just to give yourself a little cushion in case the markets keep going down? A hurricane’s coming and you go to the grocery store. Do you just buy one can of beans or get everything they are willing to give you?”

Evidence of this trend could be found in a study cited by Deutsche Bank. It estimated “the portion of marketable Treasury securities held by securities brokers is declining to levels not seen in 30 years. In the first quarter of 2015, this portion was down to around 4 percent after a peak of nearly 20 percent in 2008.” This suggested that a bottleneck could occur that “will limit equal access to all market participants even if the supply is sufficient,” said Treasury Strategies.

We asked Carfang, Why not issue more Treasuries? “The government can’t do that in an unlimited sense because of the debt ceiling. So if anyone says the debt ceiling is archaic, no, it is not. This is where it comes into play.” Secondly, he said, “during its

course of debt issuance, the government could issue more Treasury bills and fewer notes and bonds further out the yield curve.” But, he added, that is a non-starter. “The Treasury Borrowing Advisory Committee actually studied that idea and concluded the negative consequences of essentially drying up liquidity in the long-term end of the entire bond market would be worse than not having enough securities on the short end. They basically warned against printing Treasury bills.”

### Treasury Funds as Collateral

Most clearing houses will view U.S. Treasury bills as the best collateral and will trim the value of money-market funds used as collateral, said Carfang. Such haircuts are done under the assumption that T-bills and Treasury-only money-market funds are not functionally equivalent. Treasury Strategies challenges this assumption by comparing the performance of those two types of asset classes in normal and stressed conditions.

Choosing five “market-stress” events, the paper “measured the volatility of the four-week T-bills and the benchmark (Treasury) MMF for 30 days before and after the event.” The events were: the September 2008 financial crisis; the August 2011 U.S. debt-limit crisis coupled with S&P’s downgrade of the U.S. government credit rating; the November 2012 “Israel/Gaza conflict when Israel launched its week-long ‘Pillar of Defense’ initiative;” the October 2013 debt-ceiling showdown and the October 2014 “Treasury flash crash where liquidity evaporated in Treasury futures, causing prices to skyrocket and yields to plummet.”

“In every case,” Carfang told *MFR*, “the money-market funds were more stable. They had greater price stability than the four-week Treasury bill, which means they had greater preservation of value and therefore greater utility as collateral. We are saying (that) if you treat these as functionally equivalent, you’ve increased the supply of top-tier collateral.” The report estimated Treasury-only money-market fund holdings at \$231.9 billion, or “around 7 percent of the \$3.2 trillion in Treasury debt with maturities of less than one year.”

The paper concluded, “The problem of collateral scarcity is real, and the impacts are potentially devastating. Fortunately, one straightforward solution can ease pressure on collateral supply without creating undue risks in financial markets.”

Carfang said the paper is getting some traction, with inquiries for further analysis. “We had to craft an argument that would satisfy all the economic criteria and pass muster with staff economists,” he observed. ◆

### MFR COMMENTARY

Net assets of 949 Taxable MMFs rose by \$17.41 billion to \$2.458 trillion as of Sept. 29. Total Taxable Institutional fund assets increased by \$19.27 billion. Taxable Retail fund assets decreased \$1.86 billion.

The iMoneyNet Money Fund Average™/All Taxable 7-Day Yield was 0.02 percent for the 37th consecutive week. The All Taxable 30-Day Yield was 0.02 percent for the 36th straight week. The WAM shortened to 34 days from 35 days the week before.

Net assets of 377 Tax-Free and Municipal MMFs were down by \$1.63 billion, lowering their total to \$243.95 billion as of Sept. 28.

The iMoneyNet Money Fund Average™/All Tax-Free 7-Day Yield was unchanged at 0.01 percent for the 126th consecutive week. The All Tax-Free 30-Day Yield remained at 0.01 percent for the 144th straight week. The Tax-Free WAM held steady at 33 days.

A one-week increase of \$15.78 billion brought total net assets of 1,326 Taxable and Tax-Free money funds to \$2.702 trillion.

# Money Fund Report

## SUMMARY OF MONEY FUND ACTIVITY

Period Ending: 9/29/15 — Taxable Funds • 9/28/15 — Tax-Free Funds

# of Money Funds	Net Assets (\$Mils)	1-Week Change		7-Day Yield (%)	30-Day Yield (%)	Compound 7-Day Yield (%)	Compound 30-Day Yield (%)	12-Month Yield (%) (8/15)	Average Maturity (Days)
<b>Taxable Money Funds</b>									
29	54,791.4	317.3	Treasury Retail	0.00	0.00	0.00	0.00	0.00	53
29	54,474.1			0.00	0.00	0.00	0.00		52
28	12,831.8	-107.8	Treas & Repo Retail	0.01	0.01	0.01	0.01	0.00	29
28	12,939.6			0.01	0.01	0.01	0.01		28
95	119,465.6	-386.7	Govt & Agency Retail	0.01	0.01	0.01	0.01	0.01	37
95	119,852.3			0.01	0.01	0.01	0.01		38
<b>152</b>	<b>187,088.8</b>	<b>-177.2</b>	<b>Government Retail</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>41</b>
152	187,266.0			0.01	0.01	0.01	0.01		41
235	493,487.1	-1,685.3	First Tier Retail	0.01	0.01	0.01	0.01	0.01	38
235	495,172.4			0.01	0.01	0.01	0.01		39
<b>235</b>	<b>493,487.1</b>	<b>-1,685.3</b>	<b>Prime Retail</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>38</b>
235	495,172.4			0.01	0.01	0.01	0.01		39
<b>387</b>	<b>680,575.9</b>	<b>-1,862.5</b>	<b>Taxable Retail</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>39</b>
387	682,438.4			0.01	0.01	0.01	0.01		40
<b>315</b>	<b>778,327.1</b>	<b>23,830.6</b>	<b>Government Institutional</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>37</b>
314	754,496.5			0.01	0.01	0.01	0.01		38
247	998,907.7	-4,559.9	First Tier Inst	0.05	0.05	0.05	0.05	0.04	29
247	1,003,467.6			0.05	0.05	0.05	0.05		30
<b>247</b>	<b>998,907.7</b>	<b>-4,559.9</b>	<b>Prime Institutional</b>	<b>0.05</b>	<b>0.05</b>	<b>0.05</b>	<b>0.05</b>	<b>0.04</b>	<b>29</b>
247	1,003,467.6			0.05	0.05	0.05	0.05		30
<b>562</b>	<b>1,777,234.8</b>	<b>19,270.7</b>	<b>Taxable Institutional</b>	<b>0.03</b>	<b>0.03</b>	<b>0.03</b>	<b>0.03</b>	<b>0.02</b>	<b>33</b>
561	1,757,964.1			0.03	0.03	0.03	0.03		34
<b>949</b>	<b>2,457,810.7</b>	<b>17,408.2</b>	<b>Taxable (All)</b>						
948	2,440,402.5								
<b>iMoneyNet MONEY FUND AVERAGE™/Taxable (All)</b>				<b>0.02</b>	<b>0.02</b>	<b>0.02</b>	<b>0.02</b>	<b>0.02</b>	<b>34</b>
PriorWeek's Averages				0.02	0.02	0.02	0.02		35
<b>Tax-Free Money Funds</b>									
80	112,488.4	-998.6	Tax-Free National Retail	0.01	0.01	0.01	0.01	0.01	32
80	113,487.0			0.01	0.01	0.01	0.01		32
114	61,753.0	-170.4	Tax-Free National Inst	0.01	0.01	0.01	0.01	0.01	29
114	61,923.4			0.01	0.01	0.01	0.01		29
105	61,907.0	-372.9	Tax-Free State Retail	0.01	0.01	0.01	0.01	0.01	38
105	62,279.9			0.01	0.01	0.01	0.01		37
78	7,804.7	-86.2	Tax-Free State Inst	0.01	0.01	0.01	0.01	0.01	33
78	7,890.9			0.01	0.01	0.01	0.01		33
<b>377</b>	<b>243,953.1</b>	<b>-1,628.1</b>	<b>Tax-Free (All)</b>						
377	245,581.2								
<b>iMoneyNet MONEY FUND AVERAGE™/Tax-Free (All)</b>				<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>0.01</b>	<b>33</b>
PriorWeek's Averages				0.01	0.01	0.01	0.01		32
<b>1326</b>	<b>2,701,763.8</b>	<b>15,780.1</b>	<b>Grand Total - MMFs (All)</b>						
1325	2,685,983.7								

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7- and 30-day yields represent annualized results for the periods, net of management fees and expenses. 12-month yields assume reinvestment of dividends for up to one year. Money Fund Report® Compound Averages follow the calculation method approved by the SEC:

$$\text{compound average} = \left( \left\{ 1 + \frac{7\text{-day average yield}}{(100 \times 52.142857)} \right\}^{52.142857} - 1 \right) * 100$$