

## Considerations for Money Market Funds in a Rising Rate Environment

The expectation for continuous Federal Open Market Committee (FOMC) policy rate hikes throughout 2022 has institutional investors eager to see how cash may be allocated to optimize portfolios. Fed Funds Futures indicate that by year-end rates will be at or above 2%<sup>1</sup>, and the Fed's dot plot of individual Fed members' projections show a median expectation of 1.9%<sup>1</sup>. Below are some key considerations for investors in this rising rate environment.

### How quickly do interest rates react to rate hikes?

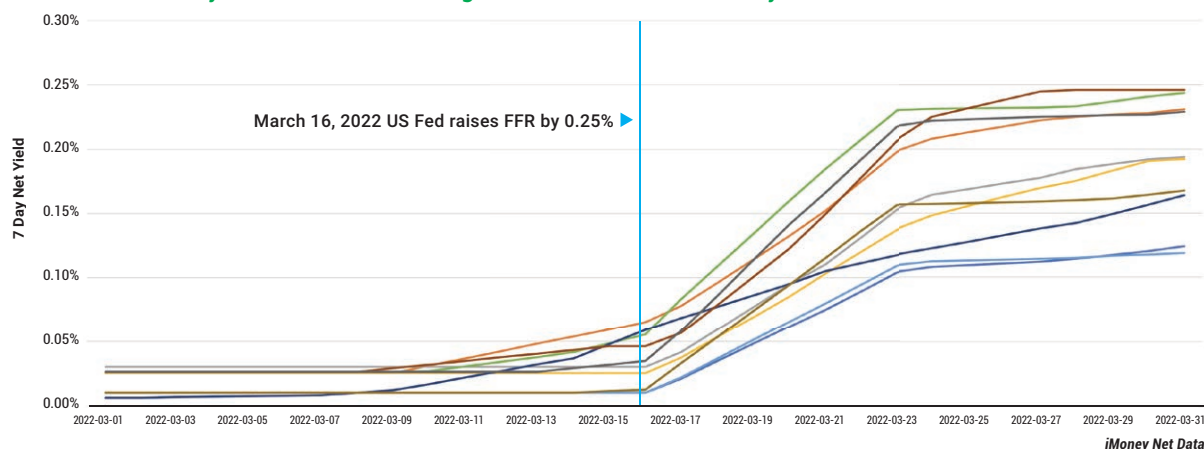
#### Where should I allocate my cash to take advantage of disparities?

Two of the most popular vehicles institutional investors use to park cash are money market funds (MMFs) and bank deposits.

While Money Market Fund Rates have been low with Fed rates on the floor, many banks have directed institutional investors to their bank deposits with more attractive interest rates or Earnings Credit Rates (ECR)s.

However, as the FOMC raises rates, money market funds are expected to be more reactive to those rate hikes than deposit products. Portfolio managers of money market funds anticipate rate hikes by investing in overnight products. This allows them to reinvest at a higher rate as soon as the Fed raises rates. The 1-day liquidity of the 10 largest government MMFs on ICD Portal averaged 87% the day of the March rate hike<sup>2</sup>.

### 7 Day Net Yields on 10 Largest US Government Money Market Funds on ICD Portal



Banks are required to maintain a certain capital adequacy ratio (CAR) and may not want excess cash on their balance sheets. The New York Times notes, "An increase in the Fed benchmark often means banks will pay more interest on deposits – but not

necessarily right away. Banks tend to raise rates when they want to bring more money in, but the largest banks already have plenty of deposits. That gives them little incentive to pay depositors more."<sup>3</sup>

<sup>1</sup> CME Fedwatch Tool as of February 17, 2022 | <sup>2</sup> iMoney Net Data | <sup>3</sup> New York Times - March 17, 2022

“Wells Fargo estimated banks will pass on about half of the increase to corporate customers after about four consecutive rate increases.”

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## Money Market Funds

MMFs have long been a favorite of treasury organizations because of their low risk, high liquidity and competitive yield. MMFs proved their fundamental strength and critical function in the aftermath of the 2008 crisis as the asset class increased in average daily balance by over 14% in the six months after Lehman collapsed<sup>4</sup>.

### New to Money Market Funds or Need a Refresher?



#### WATCH VIDEO

U.S. Institutional Money Market Funds 101

83%

of ICD clients surveyed indicated that they plan on increasing or maintaining their current level of MMF investments in 2022.

Source: 2022 ICD Client Survey

## What is my fiduciary responsibility as FOMC raises rates?

### Am I taking any unnecessary risks?

Treasury teams are tasked with an increasing amount of responsibilities and may not consider the ways in which they are violating their investment policies or over-concentrating their investments. Portfolios heavily weighted in bank deposits are therefore heavily concentrated in those banks.

Preservation of capital – or safety – is the key priority for money market funds. In contrast to bank deposits, MMFs diversify across a range of investments, mitigating risk to a single counterparty. Further, MMFs allow same day liquidity, a key requirement for treasury teams who generally are required to make fast decisions.

## What action should I take today?

### Where do I start?

Treasury teams should keep an eye on money market funds as rates change. As the industry's leading independent portal, ICD provides investors with unbiased access to over 300 global funds – 153 domiciled in the US – providing an expansive selection to suit any needs. ICD Portal provides real time access to data, such as Fund AUM, Weighted Average Maturity (WAM), Liquidity, Pricing, Net yields and Gross yields for quick decision making as the market reacts to FOMC actions.

Using ICD Portal, clients are also able to view portfolio exposures at the counterparty, currency and country levels, drilling down to the individual holdings for full transparency. Clients are not required to have a minimum investment and can purchase and redeem according to what works for them. To further manage risk and ensure conformity to investment policy, ICD Portal offers compliance rules to block trades or warn users when an action will take them out of compliance.

<sup>4</sup> Crane Data MFI Totals

To learn more about what to consider in a rising rate environment, contact your ICD Account Manager or the ICD Global Trade Desk.  
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