Deutsches Aktieninstitut

EU Money Market Fund Regulation works well – no need for reform

Response on the EU Commission's targeted consultation on the functioning of the Money Market Fund Regulation, 13 May 2022

Deutsches Aktieninstitut appreciates the opportunity to respond to the EU Commission's targeted consultation on the functioning of the Money Market Fund Regulation.[1]

The role of Money Market Funds for non-financial companies

Money market funds (MMFs) play a key role in the liquidity management of non-financial corporations. As an important cash management tool they allow corporates to deposit their short-term cash balances in a secure manner and with quick access to their funds when needed. For example, corporates use MMFs to invest their excess cash until a major expenditure, such as payroll payments or repayment of outstanding debt, is due.

In addition, MMFs have the advantage of diversifying corporates' cash deposits, thereby reducing counterparty risk. Furthermore, it is important to note that the role of MMFs has rather increased as banks are increasingly reluctant to accept short-term corporate deposits due to regulatory constraints. It is, thus, critical to ensure that corporates have viable alternatives to bank deposits for managing their cash balances.

The importance of LVNAVs and CNAVs – constant unit pricing and intra-day settling

To serve best as an efficient and cost-effective means of managing cash reserves it is important that MMFs have certain characteristics that can only be delivered by CNAVs and LVNAVs, but not or only to a limited extent by VNAVs.

Efficiency is particularly ensured when the transfer of money between non-financial companies and money market funds can take place at a constant share price that is known in advance. This for example allows for a standard processing of different money markets funds. Therefore, we welcomed the fact that under the EU regulation fund managers of CNAVs and LVNAVs can use the so-called amortized cost method to determine the unit price. The amortized cost-method generally allows funds to show a fixed share price before payments happen. Furthermore, within in certain regulatory boundaries a stable NAV of 1.00 per share can be applied.

The ability to transact on a T+0 basis at a price that is known in advance is crucial for a non-financial company. In addition, LVNAV pricing allows fund managers to price and settle at multiple points intra-day.

---

[1] This paper is based on discussions in the corporate finance/corporate treasury working group of Deutsches Aktieninstitut (EU transparency register: 38064081304-25) which is the central forum of opinion building for the treasury departments of the largest German non-financial companies.

Furthermore, from the perspective of a non-financial company as an investor in MMFs the characteristics of LVNAVs (and CNAVs) reduce price volatility of the cash management portfolio. This in turn means that the valuation of the portfolio is relatively constant and no complex accounting procedures are necessary.

And finally, LVNAVs (and CVNAVs) are typically recognised as cash or cash equivalent for accounting purposes which is not necessarily the case for other classes of MMFs.

LVNAVs and CNAVS are accepted in the market and have proven stable during the COVID-19 crisis

In particular, the important role of LVNAVs is also reflected in the data. According to ESMA[2] European LVNAVs have collected 24 percent of their investments from non-financial companies. Applying this figure to the total liabilities of LVNAVs (€ 688 billion according to ESMA) companies' investments account for ca. € 165 billion. From the perspective of non-financial investors, LVNAVs are by far the most important MMF category. They account for more than 50 percent of all MMF investments by non-financial comapnies. However, CNAVs also play an important role, even if their total market volume is significantly smaller than that of LVNAVs due to regulatory restrictions.

Moreover, we note that, according the ESMA report, during the March 2020 COVID-19 crisis, no MMF had to suspend dealings, use redemption gates, apply liquidity fees or utilise any other liquidity management tools affecting investors' ability to redeem. In other words: given that MMFs have proven sufficiently resilient to withstand this challenge, this proves that the MMF Regulation is fit for purpose.

Maintaining the LVNAV and CNAV fund structures is important for corporates – alternatives could increase systemic risk

Overall, we strongly support to maintain LVNAV and CNAV fund structures as they are important for companies for two reasons. First, the existing regulation ensures that corporates can trust in the safety of their investments which is a precondition for any instrument that is used in cash management. Second, only LVNAVs and CNAVs have specific structural features (i.e. intra-day settlement at constant share prices that are known in advance) that ensure efficient processes and easy handling.

If LVNAVs and CNAVs were not available anymore, corporate users would likely turn to second best alternatives that deliver similar characteristics. Most likely,

[2] https://www.esma.europa.eu/sites/default/files/library/esma34-49-437_finalreportmmfreview.pdf

corporates would turn to bank deposits which, however, would force corporates to increase credit limits and would lead to a concentration of counterparty risks. From an individual and systemic perspective this would mean less diversification in the cash management, less choice for corporate treasuries and less liquidity, and thus potentially higher risks.

Alternatively, corporates could turn to MMFs not domiciled in the EU, but this might come at the price of additional currency risks which in turn would increase hedging needs and costs and leads to additional administration as other products are not as standardized as MMFs. Thus, the alternative of non-EU funds regularly will be limited.

Furthermore, it has to be recognized that MMFs also play an important role in short term finance which would also be jeopardized if certain classes of MMFs were not available anymore.

There is no compelling need for action to change the Money Market Fund Regulation

Overall, we strongly support that the existing MMF Regulation has explicitly been structured in order to allow for CNAVs and LVNAVs as efficient, safe and easy-to-use means of cash management.

Changes to regulatory framework would undermine the political will of the last reform. In particular, the LVNAV class was deliberately created as a good compromise between practicability and the limitation of possible risks. The fact that the class is well accepted in the market (according to the ESMA report) shows that the reform at the time set the right course.

Contact

Dr. Gerrit Fey
Head of Capital Markets Department
Phone +49 69 92915-41
fey@dai.de

Donato Di Dio
Policy Advisor Capital Markets Policy
and Digitisation
Phone +49 69 92915-34
didio@dai.de

Frankfurt Office:
Deutsches Aktieninstitut e.V.
Senckenberganlage 28
60325 Frankfurt am Main

EU Liaison Office:
Deutsches Aktieninstitut e.V.
Rue Marie de Bourgogne 58
1000 Brussels

Berlin Office:
Deutsches Aktieninstitut e.V.
Alte Potsdamer Straße 5, Haus Huth
10785 Berlin

Lobbying Register German Bundestag: R000613
Transparency Register: 38064081304-25
www.dai.de

We want capital markets to be strong, so that they empower companies to finance great ideas and to contribute to a better future for our communities.

We act as the voice of capital markets and represent the interests of our members at national and European level.

We promote connections between our members, bringing them closer together and providing them with the most compelling opportunities for exchange.

As a think tank, we deliver facts for the leaders of today and develop ideas for a successful capital markets policy. We do this because companies, investors and society alike benefit from strong capital markets