US Rates Watch

MMF portfolio update: prime fund conversion

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MMFs see continued inflows in 2024

According to Crane data, money market fund AUM has increased $130b YTD as of Feb 13 (Exhibit 1). Gov't funds have seen $63b in inflows, prime funds have seen $70b in inflows, and muni fund AUM has declined nearly $4b YTD. While MMF inflows have continued, they have not sped up to levels seen around bank stress events in March '23, implying limited spillover from recent bank concerns (see: USD funding: limited bank stress, so far). We expect MMF inflows to continue as long as front-end rates remain elevated. Medium- to long-term, we see risk that MMF inflows slowdown or reverse as the Fed eventually cuts and the curve steepens.

Inflows into retail narrowly outpaced inst'l inflows

YTD, institutional funds have accounted for $60b in inflows while retail funds have seen $71b in inflows. (Exhibit 2). Inflows into prime institutional have outpaced gov't institutional but inflows into retail are roughly split between prime and gov't funds. Retail funds have seen steady inflows since the start of Fed hikes, driven by MMF yields rising above retail deposit rates. Conversely, institutional fund AUM was declining until bank stress events in March, which triggered robust inflows. We have not seen a repeat of this activity with recent bank headlines.

MMF yields declined as Fed cuts got priced in

The average 7-day simple yield on MMFs has declined 5bps for gov't MMFs and 6bp for prime YTD (Exhibit 4). The decline in MMF yields has been driven by Fed cuts getting priced in, starting with the first full cut priced in June, and some reduction in prime WAM. While prime fund WAMs have shortened, prime funds have been allocating more into higher yielding CP, CD, and TDs likely to compete with gov't fund yields. The spread between prime and gov't funds has been narrowing and is expected to continue as prime funds eventually implement higher liquidity requirements related to MMF reform, which will likely shift their holdings composition to more closely resemble gov't MMFs.

MMF WAM diverged with prime shortening, gov extending

Prime fund WAMs have continued to shorten YTD after peaking around 41days in mid-Dec and are now just under 33 days (Exhibit 5). Conversely, gov't funds are still extending and are 3 days longer YTD at 40.7 days. The decline in prime WAM is more significant in inst'l funds which are down 10 days from their peak vs 8 days shorter for retail. Prime fund WAM shortening is likely due to MMFs wanting to reduce risk following greater uncertainty around the Fed's cutting cycle as well as MMF reform on the horizon. In 2016 we saw a similar trend with both prime inst'l and retail WAMs shortening leading into MMF reform even as the new requirements would only impact inst'l funds. WALs have also been diverging, with prime WALs now 5.5 days shorter YTD and gov't WALs roughly 2.6 days longer (Exhibit 6).

Abbreviations:
AUM: Assets under management
CD: Certificate of deposit
CP: Commercial paper
DL: Debt limit
DVP: delivery versus payment
FHLB: Federal Home Loan Banks
FICC: Fixed Income Clearing Corp
GC: General Collateral
Gov't: Government
Inst'l: institutional
MMF: Money market fund
ON RRP: Overnight reverse repo facility
QT: Quantitative tightening
QTD: Quarter to date
TD: Time deposit
UST: US Treasuries
WAL: Weighted average life
WAMs: Weighted average maturity
YTD: Year to date

Declining MMF ON RRP take-up has slowed

As of Jan month-end, MMFs still made up 95% of ON RRP take-up, in line with the last few month-ends. Take-up declined over January with avg take-up around $634b ex month-end vs $797b in December (Exhibit 7). ON RRP take-up is an additional $62b lower since January, implying the pace of RRP decline has slowed. The number of counterparties at ON RRP has also declined from an average of 100 per day from Jan to Oct '23 to only 78 per day from Jan 2 '24 though today. This decline has recently tapered out but overall, the lower number of counterparties implies that several MMF no longer need to use the Fed ON RRP as an investment option of last resort due to higher levels of money market supply.

The downward trend in ON RRP take-up has been driven by bill issuance and higher yielding front-end rates, especially around large collateral settlements. The trend in ON RRP take-up is important for our QT forecasts as we expect the Fed to slow the pace of UST redemptions once ON RRP is relatively low (see latest balance sheet forecast here: Fed balance sheet: tax date tweaks). We expect MMFs will continue to move cash out of ON RRP, especially if banks continue to compete for funding and front-end rates cheapen.

MMFs shifted holdings out of UST repo

MMF holdings of bills increased $209b in Jan, nearly two times net new bill issuance (Exhibit 10). At the same time, MMF holdings of UST notes were flat but declined $33b for FRNs (Exhibit 11). Demand from MMFs to move further out the curve appeared to reverse as uncertainty around Fed rate cuts grew.

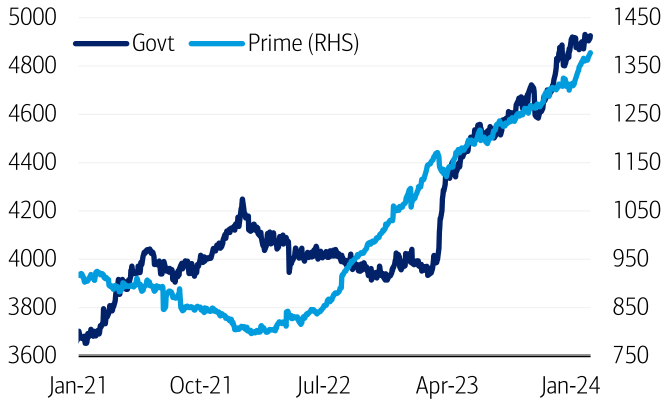
Government MMFs saw $49b in inflows in January and reduced their investment in UST repo by $141, which largely came out of ON RRP (Exhibit 12). Gov't funds shifted their holdings primarily into Treasury debt, as well as agency debt and agency repo. Prime funds similarly saw $48b in inflows in Jan and reduced their allocation to UST repo by $84b but shifted their holdings into non-negotiable TD, Treasury debt, CD and financial CP (Exhibit 13).

Money market fund FICC-sponsored repo activity increased nearly $20b in Jan, primarily through agency repo (Exhibit 14). Based on our estimates using Crane MMF holdings and DTCC FICC sponsored volumes, MMFs currently comprise 76% of FICC sponsored reverse repo volumes (Exhibit 15). The regulatory changes around central clearing of UST repo, which must be adopted by Jun 2026, will lead to higher sponsored repo volumes going forward.

MMF regulatory changes on the horizon

MMF reform was back on client's radars last week after Capital Group announced its largest prime institutional MMF would be converted to a government MMF. Recall, a government MMF is required to invest at least 99.5% of total assets in cash, government securities or repo collateralized by cash or government securities. The latest round of MMF reform involves the implementation of liquidity fees around large redemptions for prime institutional MMFs (not gov't funds) which are required to comply by October 2 2024 (see SEC MMF final rule: better than feared). Liquidity fees are expected to deter some investors from keeping their cash in a prime inst'l fund. As a result, we expect to see more prime funds convert to gov't as well as further consolidation of prime inst'l funds.

Exhibit 1: MMF AUM ($bn)
Prime fund inflows outpaced gov't funds YTD



Source: BofA Global Research, Crane Data

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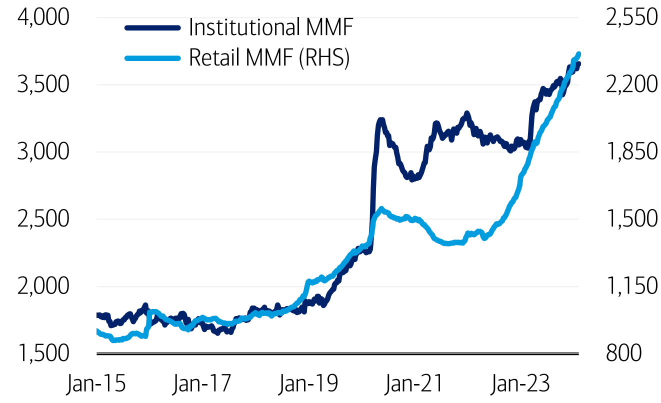
Exhibit 2: Institutional MMF AUM vs Retail MMF AUM ($tn)
Retail funds continued to see steady inflows YTD



Source: Bloomberg, ICI

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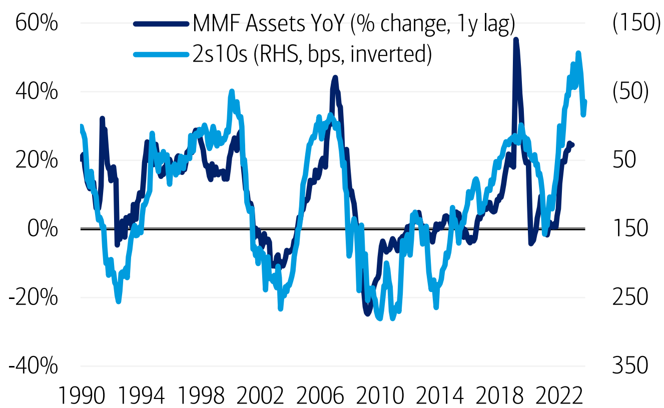
Exhibit 3: MMF assets and 2s10s curve
As 2s10s curve steepens, MMFs inflows slow or even reverse



Source: BofA Global Research, Bloomberg

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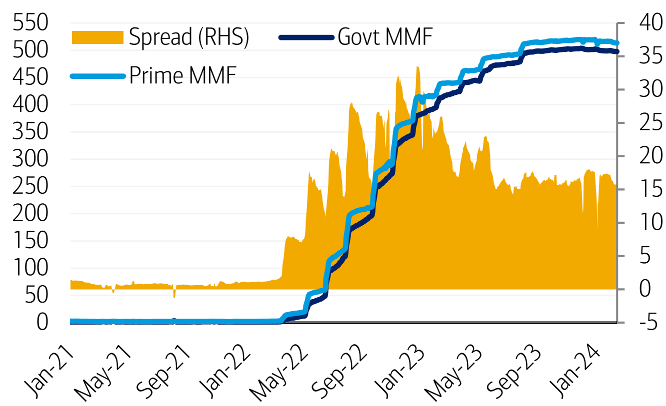
Exhibit 4: Domestic MMF 7 day simple yield (bps)
MMF yields have begun to decline as cuts get priced in



Source: BofA Global Research, iMoneyNet

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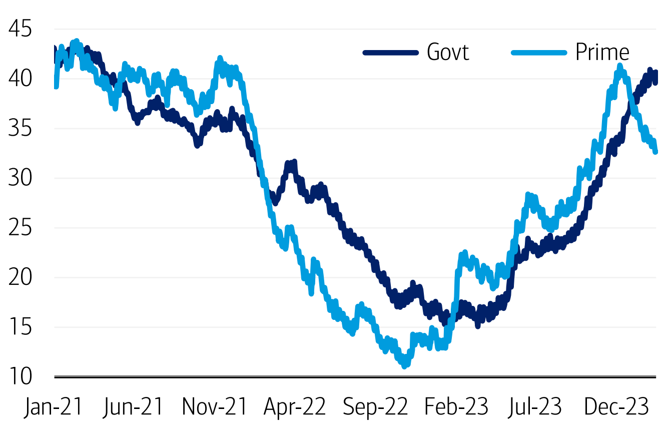
Exhibit 5: MMF WAM (Days)
Prime WAMs have shortened over 5 days YTD. Gov't funds 2 days longer



Source: BofA Global Research, iMoneyNet

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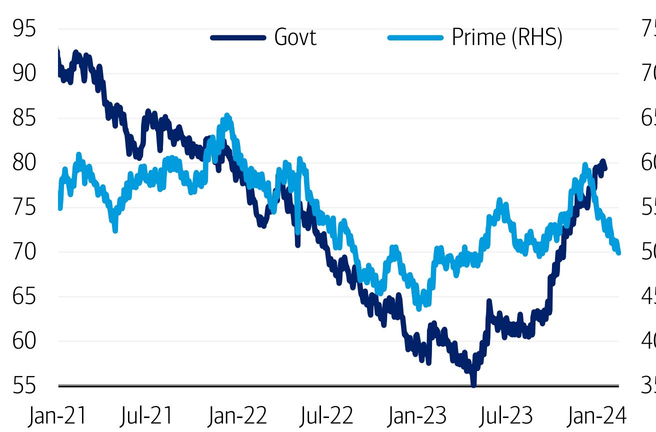
Exhibit 6: MMF WAL (Days)
Prime WAL declined 5.5 days YTD vs gov't fund WAL longer by 2.6 days



Source: BofA Global Research, iMoneyNet

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Exhibit 7: Top 10 MMFs' ON RRP use ($bn)
MMF ON RRP declined from Dec but still comprise 95% of RRP take-up

Fund	Jan Assets	Jan ON RRP	Dec ON RRP	Nov ON RRP	Oct ON RRP
Vanguard Federal Money Mkt Fund	297	61	65	71	77
Fidelity Govt Money Market	323	50	70	41	56
Fidelity Inv MM: Govt Port	200	40	44	29	36
Fidelity Cash Central Fund	52	39	37	39	37
Fidelity Govt Cash Reserves	238	37	49	29	40
Schwab Treasury Oblig MF	69	25	31	37	45
JPMorgan US Govt MM	264	24	26	48	75
Fidelity Inv MM: Treas Port	63	22	25	21	26
Vanguard Cash Reserves Federal MM	120	20	23	24	26
Northern Instit Treasury MMkt	86	19	25	28	34
Total of all MMFs		584	967	844	1077

Source: BofA Global Research, Crane Data

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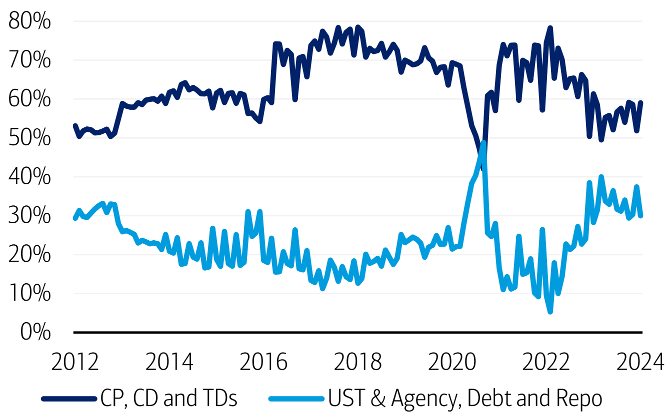
Exhibit 8: Prime MMF holdings as % of total
Prime funds allocated more into UST debt but greatly reduced UST repo



Source: BofA Global Research, iMoneyNet

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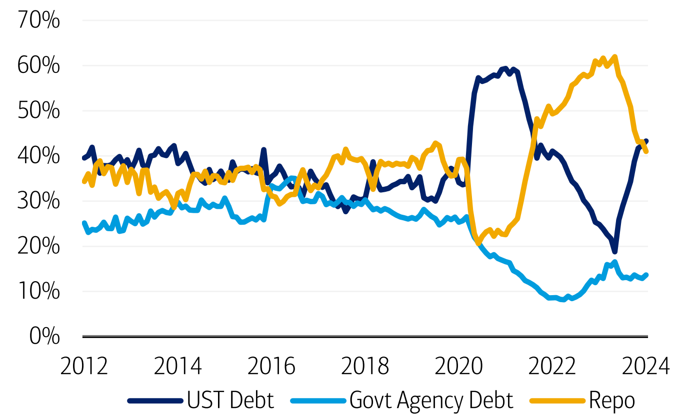
Exhibit 9: Govt MMF holdings as % total
Gov't funds shifted out of UST repo, into UST debt



Source: BofA Global Research, iMoneyNet

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Exhibit 10: Bills outstanding versus total MMF holdings ($bn)
Bill holdings jumped in Jan

	Bills Outstanding	MMF Holdings	MMF as % Total
Sep-22	3645	759	21%
Oct-22	3666	762	21%
Nov-22	3812	704	18%
Dec-22	3697	595	16%
Jan-23	3939	658	17%
Feb-23	4058	642	16%
Mar-23	4069	662	16%
Apr-23	3943	653	17%
May-23	3993	570	14%
Jun-23	4467	882	20%
Jul-23	4771	1116	23%
Aug-23	5074	1268	25%
Sep-23	5260	1413	27%
Oct-23	5457	1633	30%
Nov-23	5671	1846	33%
Dec-23	5676	1790	32%
Jan-24	5780	1999	35%

Source: BofA Global Research, Crane Data

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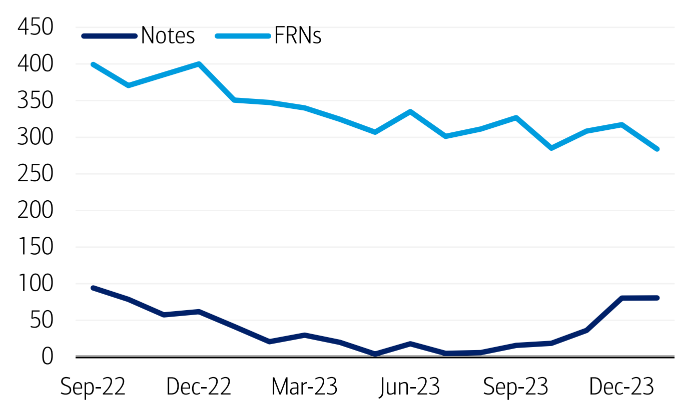
Exhibit 11: MMF holdings of Treasury notes and FRNs
MMF holdings of notes unchanged in Jan, declined $33b for FRNs



Source: BofA Global Research, Crane Data

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Exhibit 12: Domestic MMF holdings, government funds ($bn)
Gov't MMFs increased allocations to UST debt but reduced UST repo

	Government			Government Institutional			Government Retail		
	Jan-24	MoM Δ	YoY Δ	Jan-24	MoM Δ	YoY Δ	Jan-24	MoM Δ	YoY Δ
Cash	83.6	14	30	61.7	9	21	21.9	5	9
Treasury Debt	2136.4	67	1153	1248.2	22	491	888.2	45	662
Treasury Repo	1390.3	(141)	(643)	601.2	(76)	(323)	789.1	(65)	(320)
Govt Agency Debt	674.1	45	144	358.4	5	107	315.6	40	38
Govt Agency Repo	627.0	55	276	467.4	42	206	159.7	13	71
Other Repo	5.5	4	3	5.5	4	3	0.0	0	0
Investment Co Funding Agrmnt	13.5	4	5	8.0	4	5	5.5	(0)	0
VRDN	0.7	0	0	0.1	(0)	0	0.6	0	0
Other Instrument	3.2	3	2	1.5	1	1	1.7	2	1
Total	4934	49	970	2752	10	510	2182	40	461

Source: BofA Global Research, iMoneyNet

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Exhibit 13: Domestic MMF holdings, prime funds ($bn)
Prime MMFs shifted out of UST repo but into UST debt, TD, CP, and CD

	Prime			Prime Institutional			Prime Retail		
	Jan-24	MoM Δ	YoY Δ	Jan-24	MoM Δ	YoY Δ	Jan-24	MoM Δ	YoY Δ
Cash	19.6	1	9	5.9	0	1	13.7	0	8
Treasury Debt	53.3	22	45	4.6	(1)	1	48.7	23	44
Treasury Repo	136.6	(84)	(18)	24.1	(22)	(12)	112.5	(62)	(5)
Govt Agency Debt	1.6	(0)	0	0.8	(0)	0	0.8	0	0
Govt Agency Repo	111.7	5	64	12.0	(4)	4	99.7	9	60
Other Repo	72.9	6	23	35.9	3	7	37.0	3	16
CD	221.0	18	62	67.4	6	3	153.6	12	59
Financial Co CP	164.2	10	19	48.7	4	(9)	115.6	7	28
ABCP	69.0	6	23	23.2	2	7	45.8	4	17
Other CP	14.7	5	(2)	4.5	1	(1)	10.2	4	(1)
Non-Negotiable TD	128.1	58	35	54.1	30	10	74.0	28	24
VRDN	8.0	0	2	1.9	(0)	0	6.1	0	2
Other	7.0	0	(1)	0.0	0	0	0.0	(74)	0
Total	1011	48	261	287	19	8	724	29	253

Source: BofA Global Research, iMoneyNet

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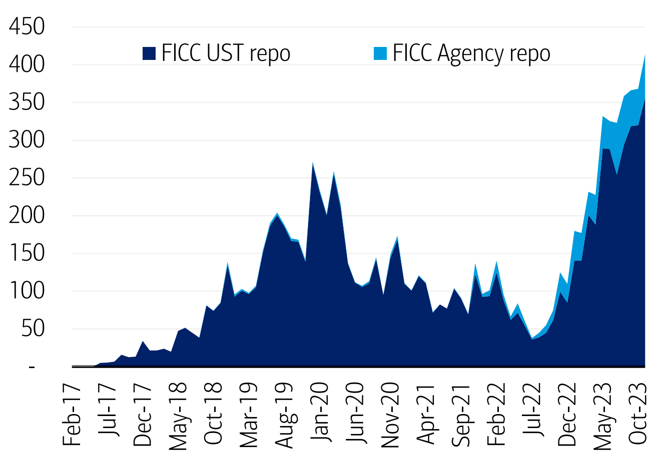
Exhibit 14: MMF FICC repo by collateral
MMF FICC repo is currently 86% UST and 14% Agency



Source: BofA Global Research, Crane Data

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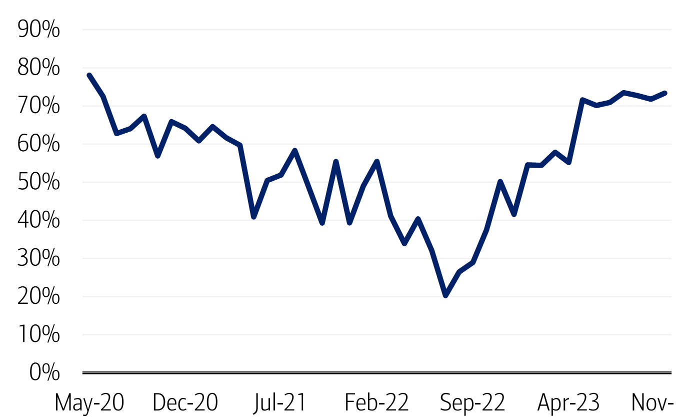
Exhibit 15: MMF FICC repo as a % of FICC sponsored reverse repo volumes
MMFs are currently 76% of FICC sponsored reverse repo volumes



Source: BofA Global Research, Crane Data, FICC DTCC

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