The Carfang Group

May 14, 2021

Vanessa Countryman, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Request for Comment on Potential Money Market Fund Reform Measures in President's Working Group Report, File No. S7-01-21

Dear Ms. Countryman:

The Carfang Group[1] appreciates the opportunity to offer comments in response to the Commission's release of the December 2020 President's Working Group on Financial Markets, Overview of Recent Events and Potential Reform Options for Money Market Funds ("PWG Report").

We applaud all efforts to enhance the U.S. capital markets, already the broadest, deepest and most liquid in the world. We especially encourage policies that facilitate the efficient flow of working capital to corporations and municipalities, the engines of economic growth, job creation and infrastructure funding. Efficient flow of capital between investors and issuers is paramount.

The Carfang Group strongly encourages the Commission, and more broadly, all financial regulators, to avoid premature rule making until (1) the totality of the multi-trillion-dollar capital flows during the March 2020 crisis are examined, (2) the roles that all market participants and regulators played are understood, and (3) the efficacy of the trillions of dollars of government support across the financial markets and institutions is evaluated.

Some of the failures, shortcomings and omissions of the PWG Report have been documented.[2] [3] [4] [5] Those papers and others demonstrate why the report should not be relied upon as the basis of yet another round of regulation of Prime Money Market Funds (PMMFs) at this time.

[1] The Carfang Group is a leading consultant in the areas of treasury, banking and liquidity management. www.thecarfanggroup.com.
[2] Institutional Cash Distributors (ICD), "ICD Data Shows No 'Run' on Prime Money Market Funds Last March", available at https://icdportal.info/resources/icd-data-shows-no-run-on-prime-money-market-funds-last-march/.
[3] Investment Company Institute, ICI Viewpoint, "On Closer Look, a Very Different Picture of Funds' Role in the Commercial Paper Market", available at https://www.ici.org/viewpoints/21_view_mmf1.
[4] The Carfang Group, "Corporate Treasurer Response to March Market Collapse"", available here.
[5] Division of Investment Management's Analytics Office of the U.S. Securities and Exchange Commission (SEC), "Prime MMFs at the Onset of the Pandemic: Asset Flows, Liquidity Buffers, and NAVs", available at https://www.sec.gov/files/prime-mmfs-at-onset-of-pandemic.pdf

The purpose of this letter is to move beyond the limitations of the PWG Report and set out the appropriate **strategic** context[6] for examining the pandemic induced market turmoil of early 2020.

The Problem to Be Solved

The Carfang Group defines the strategic questions as follows:

- What were the systemic risks in play during the crisis and what role did each of the market participants play? Did PMMFs play any material role?
- At what cost to market resilience should risks, systemic or otherwise, be eliminated or reduced?
- Can a market increasingly dominated by central banks remain truly resilient?

Crisis-Related Market Turmoil in Perspective

PMMF redemptions represented only 6% of the money in motion during the March 2020 crisis.

- $125 billion exited PMMFs during the crisis.
- $1.086 trillion surged into domestic deposits of U.S. banks.
- Government and Treasury money funds saw $892 billion historic new inflow.
- Thus, $1.978 trillion was in flight and only $125 billion (6%) of that came from PMMFs. The rest was in flight from somewhere else. Where?
- $125 billion is a large number but it needs to be examined in context of all the money that was in flight at the time. Understanding the other 94% would be important before instituting new regulations.

Since the implementation of the 2014 regulations, PMMFs' role had already been significantly diminished to just 5% of the liquidity market.

- In 2016, PMMF assets were 10.2% of M3, the institutional measure of U.S. money supply.
- At the beginning of 2020 before the onset of the pandemic in the U.S., PMMF share had been cut in half to just 5.0%.
- Can 5% of anything be considered systemic?

[6] For a statistical summary of capital market flows and trends since the implementation of the 2014 money fund regulations through the pandemic market crisis, visit https://tinyurl.com/carfanggroup-mmf-liquidity.

It's in this context that we noted the PWG Report's attempt to deceptively suggest that PMMFs played a major role in the crisis. "Prime and tax-exempt MMFs were not the sole contributors to the pressures in short-term funding markets. However, it appears that MMF actions were particularly significant relative to market size." That is grossly misleading.

PMMF liquidation of just 3% of the outstanding commercial paper (CP) in March 2020 was not a crisis accelerant.

- On Feb. 19, 2020, the day the S&P 500 peaked before it's pandemic selloff, outstanding CP totaled $1.123 trillion according to the St. Louis Fed.
- Between Feb. 19 and Mar. 18, the day that the Money Market Liquidity Facility (MMLF) was established, outstanding CP actually *rose* by $24 billion to $1.147 trillion.
- The PWG Report notes that PMMFs liquidated $35 billion of CP over the period in which CP outstanding actually *increased* and then incorrectly concluded that was somehow problematic.
- In the year prior to the crisis, daily CP issuance fluctuated but averaged $79.8 billion/day. Total CP liquidation by PMMFs during the entire crisis was less than one half of one day's issuance. That could hardly be deemed disruptive.
- There were clearly issues in the $1.1 trillion commercial paper market during the crisis. However, the impact related to PMMFs was de minimis.

PMMFs, once again, weathered this crisis as the most resilient non-government backed asset class.

- Feb. 19, 2020 - As Covid concerns swept the globe, both the S&P 500 and the NASDAQ reached their pandemic peaks and began their declines.
- Mar. 5 - The ICE/BofA 1 – 3 year corporate bond index and it's similar 5 – 7 yr. index peaked and began their declines.
- Mar. 6 - The ICE/BofA 15 year corporate bond index peaked and began its decline.
- Mar. 9 - After holding steady throughout the period, assets in PMMFs finally began to decline. Both the S&P 500 and the NASDAQ had *already plunged by 19%.*

- Mar. 23 is arguably the market bottom. By that point:
  - S&P had declined 34%, NASDAQ declined 30%
  - ICE/BofA 15 year had declined 24%
  - ICE/BofA 5 - 7 year had declined 12%
  - ICE/BofA 1 - 3 year had declined 6%
- By contrast, the worst performing PMMF maintained a solid 99.76 cents on the dollar. The median performance was an even better 99.92.

All short-term asset classes, public and private sector alike, received trillions of dollars in financial support and/or regulatory forbearance during the crisis.

- The PWG Report implies that the $48 billion of MMLF relief for PMMFs is a stigma whereas the other several trillion of support to other sectors was just prudent exercise of the Fed's "lender of last resort' role.

- In grossly misleading fashion, the PWG Report asserts "Beyond the MMLF, several other Federal Reserve actions and announcements in March *likely* contributed to these improved conditions." (Italics are mine)
- The Fed instituted the Secondary Market Corporate Credit Facility (SMCCF) in March, an unprecedented secondary market facility to purchase up to $750 billion of corporate debt and support that market.
- In March alone, the Fed's money market asset purchases ballooned its balance sheet by $1.6 trillion. It subsequently bailed out markets with another $1.5 trillion since then. Its purchase of government securities has supported the U.S. government bond market to the benefit of the largest holders of government securities including commercial banks, government money funds, ETFs and bond funds.
- Fed bond buying continues even today at a rate of $120 billion per month ($1.44 trillion/year).
- G-SIBs, the systemically important banks, received a waiver from Basel III Supplemental Leverage Ratio requirement, creating over $1 trillion of new deposit taking capacity at just a handful of the largest U.S. banks.
- Even reserves of the FDIC, the insurer of over $8 trillion in bank deposits, were allowed to fall below the statutory minimum set by Dodd-Frank.
- The reality is that although helpful, the **$48 billion MMLF was barely a rounding error** in the several trillion dollars of support provided by the government.

Conclusion

The scope of the PWG Report is far too narrow to provide a useful framework for enacting new regulations on PMMFs.

This letter provides important context and perspective that was absent from the PWG Report.

- PMMF share of short-term liquidity in the U.S. was cut in half by the 2014 MMF regulations to just **5%**.
- PMMF outflows represented only **6%** of the money flows set in motion by the crisis.
- PMMF liquidation of CP during the crisis represented only **3%** of the CP outstanding.
- The MMLF support for PMMFs was barely **1%** of the total crisis support that the government provided to other money market participants.

Before rushing into premature decisions, regulators need to understand

(1) the totality of the multi-trillion-dollar capital flows during that period,

(2) the roles that all market participants and regulators played, and

(3) the efficacy of the trillions of dollars of government support across the financial markets and institutions.

The Carfang Group is pleased to present our findings and look forward to supporting the Commission as it seeks to further enhance the already globally preeminent U.S. capital markets. We would be please to discuss this further or answer any questions you may have.

Respectfully submitted,

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