

## Fitch: Fed Reverse Repos Not Only About Rates for Money Funds

Written by Australian Business

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NEW YORK--( [BUSINESS WIRE](#) )--Money market funds (MMFs) may be more willing to rely on the Federal Reserve for future funding if the Fed's new overnight reverse repo facility becomes a more permanent fixture in money markets, Fitch says.

If the Fed's facility becomes permanent and allows a full allotment allocation to eligible counterparties, we believe money funds will increase reliance on the facility and allocate larger amounts on a consistent basis. This could change the current environment in which money funds seek to maintain relationships with dealers even at below-market rates as a hedge against limited supply.

At year-end 2013, a time of very limited supply of money market instruments, 102 eligible counterparties lent the Fed \$197.8 billion at a rate of 3 basis points set by the Fed. According to Crane Data, MMFs accounted for \$139.2 billion of this amount. This exposure represented 7.1% of government money fund assets, 6.8% of Treasury funds and 4.7% of prime funds.

While the amounts of repo done with the Fed represent relatively large portions of money fund assets, the data also shows that money funds were willing to transact repo with other counterparties at the same, or lower, rates than with the Fed. As of the same date, taxable money funds transacted a total of \$148.9 billion of overnight repo backed by Treasury or agency securities with counterparties other than the Fed for rates between 0 and 3 basis points.

This dynamic may be partially explained by the Fed's eligibility criteria, which require that a money fund have net assets of at least \$5 billion for six months before being able to participate in the Fed's reverse repo facility. Indeed, 82 money funds did not meet the eligibility requirements and accounted for \$24.8 billion of overnight government repo at or below 3 basis points. Further, 20 money funds participated in the Fed's facility to the full extent permitted (\$3 billion), and were forced to invest \$60.1 billion of remaining funds in repo with non-Fed counterparties at 0 to 3 basis points.

However, 59 money funds that met the Fed's eligibility criteria did not participate in the Fed's facility, or did so partially without exceeding the \$3 billion counterparty limit, yet they invested \$63.7 billion in overnight government repo with non-Fed counterparties at rates of

3 basis points or less.

This segment exemplifies the importance of maintaining access to repo supply even at disadvantageous rates. Fund managers employing this strategy may fear that if they invest with the Fed instead of with their regular repo counterparties, these counterparties would be less willing to allocate investments to the funds in the future. As the Fed's repo facility is not yet permanent, it may not be viewed as a reliable long-term source of supply.

The Fed has been taking steps to build additional confidence in the reverse repo facility and encourage participation. The Fed recently extended the testing phase of the facility by one year to January 2015, and has been continuously increasing the counterparty bid limit, up to \$7 billion currently from \$500 million at the program's inception.

For more information on this topic, please see the report titled, 'U.S. Money Market Funds Dashboard 4Q13', available at [www.fitchratings.com](http://www.fitchratings.com).

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The above article originally appeared as a post on the Fitch Wire credit market commentary page. The original article, which may include hyperlinks to companies and current ratings, can be accessed at [www.fitchratings.com](http://www.fitchratings.com). All opinions expressed are those of Fitch Ratings.

Applicable Criteria and Related Research:

U.S. Money Market Funds Dashboard 4Q13

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