BETTER MARKETS

– FACT SHEET –

Money Market Funds Are Failing and Being Bailed Out Again, As They Were During the 2008 Financial Crisis Just Twelve Years Ago

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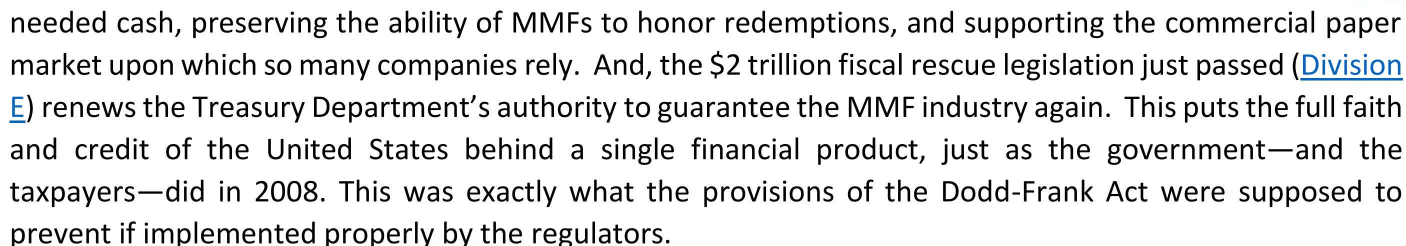
Another devastating financial and economic crisis is engulfing the nation just twelve years after the last one in 2008. The first priority must be to respond as fully and effectively as possible with measures that will enable tens of millions of Americans to meet their daily needs while minimizing damage to the economy. We also need to plan for next steps. But it's also important to look at what is happening today, identify troubling similarities with the last crisis, and ask why we are repeating the mistakes of the past.

A dramatic case in point is the money market fund ("MMF") market, which once again is teetering on the brink of failure. The MMF market nearly collapsed during the 2008 crisis and would have but for a massive, industry-wide, taxpayer-guaranteed backstop of the entire $3.4 trillion industry—the first time such action was taken in the nation's history. Remarkably, now, just twelve years later, it is happening again. That's because, following the 2008 crash, regulators and policymakers failed to sufficiently reform the MMF markets. Responding to relentless industry lobbying, they instead enacted half-measures, and one lesson is clear: Strong regulatory oversight is essential, not only in the MMF market but across the financial system, and our regulators and policymakers have to get it right or hardworking American taxpayers will inevitably suffer. Here are the facts:

<u>Today's crisis is again putting MMFs on the brink of collapse due to prior regulatory failures</u>.

- It is no surprise that MMFs are once again experiencing a huge surge of withdrawals and facing dangerous instability, intensifying the crisis that is now unfolding throughout the financial system. That's because in every crisis there is a flight to safety (U.S. dollars); there is precipitous de-leveraging by virtually everyone; and individuals and companies need cash quickly. The first place they turn is their MMF accounts, which misleading suggest that they cannot lose money and will never "break the buck."
- The result? Numerous recent reports indicate that the assets of prime MMFs have dropped dramatically. For example, ICI data shows that prime MMF assets overall dropped by $85.38 billion, or over 10%, just between March 4 and March 18, 2020. Some funds are faring much worse, with their assets falling by half as investors withdraw. And many MMF sponsors are being forced to backstop their MMFs with cash infusions to prevent them from "breaking the buck" as they sell assets to meet redemptions when all asset classes are falling in value. Among the most prominent sponsors forced to provide this support are Goldman Sachs and BNY Mellon.
- The situation has become so grim that on Wednesday, March 18, 2020, the Federal Reserve established an emergency lending facility so that banks could buy more assets from prime funds, thus injecting desperately



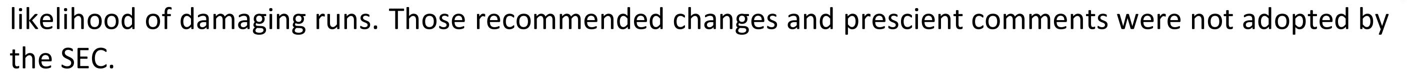
needed cash, preserving the ability of MMFs to honor redemptions, and supporting the commercial paper market upon which so many companies rely. And, the $2 trillion fiscal rescue legislation just passed (Division E) renews the Treasury Department's authority to guarantee the MMF industry again. This puts the full faith and credit of the United States behind a single financial product, just as the government—and the taxpayers—did in 2008. This was exactly what the provisions of the Dodd-Frank Act were supposed to prevent if implemented properly by the regulators.

The 2008 crisis crashed the MMF market, which would have collapsed but for a huge taxpayer bailout.

- In the early days of the 2008 crisis, a prominent MMF experienced a wave of redemptions, famously broke the buck, sparked a panic, triggered a run on prime MMFs, and precipitated a liquidity crisis in the short-term wholesale funding market. In response, and for the first time in history, on September 19, 2008, the Treasury Department and the Federal Reserve were forced to implement a series of emergency measures effectively guaranteeing the entire $3.4 trillion money market fund industry. Effectively, every U.S. taxpayer was put on the hook for the MMF industry.
- These actions from the first days of the 2008 financial crisis vividly illustrated the fact that MMFs are systemically significant and can spread destabilizing risk rapidly throughout our financial system. In truth, MMFs have long been an investment product masquerading as a guaranteed banking product, and they can trigger and intensify a financial crisis unless they are properly regulated. Put differently, MMFs are really no different than bank accounts except that bank accounts are cash and insured by the Federal government (in exchange for a fee and very careful regulation to protect taxpayers) whereas MMFs are not insured and are not cash, but invested in a variety of cash-like financial instruments.
- In fact, the collapse of the MMFs in 2008 was not the first time—or the last—when MMFs faced significant stresses and potential collapse. Over the years, many MMFs would have broken the buck had it not been for sponsor support.

The SEC's regulatory response was little more than inadequate half-measures.

- The SEC's response to the MMF crisis was incremental and incomplete. As a first step, in 2010, the SEC strengthened the liquidity, credit quality, and maturity standards governing MMF portfolio investments. While these were important measures, they came nowhere near the required response.
- The SEC resisted any further reforms. But the need for more safeguards against MMF instability was so clear that in November 2012, the FSOC, by unanimous vote, took the extraordinary and unprecedented step of issuing "Proposed Recommendations" directed to the SEC, setting forth necessary structural MMF reforms that would reduce the risk of destabilizing runs. Those proposals included the essential reform of floating the net asset value or "NAV" and, significantly, a ***capital buffer***. Better Markets strongly supported those proposals, which you can read about in detail here.
- The FSOC's 2012 recommendations prompted the SEC to act, but the result was a handful of piecemeal and insufficient reforms in July of 2014. The SEC essentially (1) required institutional MMFs to float their NAVs (while excluding ***two-thirds*** of all MMFs from this requirement), and (2) gave MMFs ***discretion*** to require the imposition of liquidity fees and redemption gates whenever weekly liquid assets dropped below certain levels. The SEC declined to adopt a capital buffer requirement, turning a blind eye to the reality that bank deposit-like MMFs called for banking-style safeguards.
- Better Markets strongly supported these measures as well, but strenuously urged the SEC to go much further, arguing that the SEC should float the NAV for ***all*** funds to mitigate run risk, promote transparency, and treat all investors more fairly. We also urged the SEC to require MMFs to maintain capital buffers that could absorb significant losses, thus promoting stability, instilling investor confidence, and reducing the



likelihood of damaging runs. Those recommended changes and prescient comments were not adopted by the SEC.

<u>As a result, taxpayers are on the hook again and the lesson is clear: Fix the problem once and for all.</u>

- Once again, American taxpayers, via the Treasury Department and the Federal Reserve, are being forced to bail out the entire MMF industry, this time because policymakers and regulators failed to do their jobs, failed to learn obvious lessons from just 12 years ago, and failed to shore up a weak regulatory framework that has once more—predictably—put the financial system at risk.
- After the current crisis subsides, those leaders must close the regulatory gaps in the MMF markets once and for all—and address any other regulatory failures and weaknesses that this still-unfolding calamity reveals.

Better Markets is a public interest 501(c)(3) non-profit based in Washington, DC that advocates for greater transparency, accountability, and oversight in the domestic and global capital and commodity markets, to protect the American Dream of homes, jobs, savings, education, a secure retirement, and a rising standard of living.

Better Markets fights for the economic security, opportunity and prosperity of the American people by working to enact financial reform, to prevent another financial crash and the diversion of trillions of taxpayer dollars to bailing out the financial system.

By being a counterweight to Wall Street's biggest financial firms through the policymaking and rulemaking process, Better Markets is supporting pragmatic rules and a strong banking and financial system that enables stability, growth and broad-based prosperity. Better Markets also fights to refocus finance on the real economy, empower the buyside and protect investors and consumers.

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