The Association of Corporate Treasurers

Comments in response to

Moody's proposed New Money Market Fund Rating Methodology and Symbols

Moody's Investors Service,

September 2010

5 November 2010

The Association of Corporate Treasurers (ACT)

The ACT is a professional body for those working in corporate treasury, risk and corporate finance. Further information is provided at the back of these comments and on our website www.treasurers.org.

Contact details are also at the back of these comments.

We canvas the opinion of our members through seminars and conferences, our monthly e-newsletter to members and others, *The Treasurer magazine*, topic-specific working groups and our Policy and Technical Committee.

General

The ACT welcomes the opportunity to comment on this matter.

This document is on the record and may be freely quoted or reproduced with acknowledgement.

Response

Moody's is proposing a new rating methodology and a new ratings scale for money market funds (MMFs). Historically Moody's have used a slightly modified version of their traditional long-term scale (Aaa to C) in rating MMFs, however the nature of MMFs differs from long-term instruments. Whilst MMF investors own shares in the fund, the expectation is that they can withdraw their funds on demand. Moody's is proposing a new rating scale from MF1+ to MF4, with MF1+ exhibiting a risk profile broadly consistent with Prime-1 rated investments. The proposed ratings are aimed at measuring the effectiveness of a MMF meeting investor objectives, namely (i) preserve principal; and (ii) provide liquidity.

We have been asked to provide feedback on the proposal and new rating scale, together with feedback on the following questions:

1. *Would money markets benefit from fund ratings that provide enhanced information and greater differentiation as we (Moody's) are proposing?*

   The ACT believes that any form of greater transparency is good news for investors. Treasurers recognise that money market funds are different from other investment instruments and that a separate rating scale would be a good thing as it incorporates the additional risks, including liquidity and redemption risk.

2. *Would the approaches proposed and the factors considered, including the relative emphasis on and calibration of – the different factors, provide a reasonable basis for differentiation among money market funds?*

   We have provided comment and agree with your focus on the following risks:

   - Portfolio credit profile. The credit quality of individual investments within the fund and the maturities of those investments must remain a core part of the credit rating process for a MMF. Your diagram 6 shows how you would combine the credit profile with stability profile to reach the MF rating. It appears that these two drivers are broadly speaking given equal weight. Incorporating portfolio stabilities is a welcome move but even so we wonder whether the underlying credit strength of the portfolio should remain the predominant driver of the overall rating. We note that to a small extent credit profile will contribute into the stability profile through the market risk stress factor.
   - Liquidity risk is a key differentiator of MMFs. The investor assumption is that funds can be withdrawn on demand, hence it is helpful to build into the methodology an understanding of investor concentration and liquidity ratios.
   - Redemption risk is included in the derivation of the Fund liquidity as part of the Portfolio Stability Profile. Whilst the calculation incorporates the concentration of fund shareholders, it does not include the nature of these shareholders. Where the nature of shareholders would impact an investor's decision e.g. they constantly dip in and out of funds, then this should be factored in.

- Asset profile and exposure to market risk form part of your stability scorecard and this appears a reasonable approach.
- Sponsor support is to be included in your qualitative assessment and will consider the sponsor's ability and willingness to provide support as regards principle and liquidity. In the absence of any formal contractual obligation this is inevitably subjective, but can nonetheless be attempted using the considerations you have identified. We are aware that companies already take account of the sponsor name (often looking to their key relationship banks) in deciding which MMF to invest in but we do wonder if this aspect can sometimes be given a disproportionate weighting in the overall assessment. We would welcome commentary as to the perceived level of sponsor support in the credit rating report.

Certain MMFs do not offer same day liquidity but rather allow redemptions at several days notice, which allows them more flexibility to invest for longer periods. It may be that funds will also start to introduce specific provisions to limits redemptions if it would prejudice other investors. Both features limit liquidity for investors but thereby hope to limit any enforced capital losses. Presumably any rating assessment will take into consideration these sorts of features and be subject to different liquidity parameters in your stability scorecard.

3. *Would the use of distinct rating symbols, along with added disclosure about rating drivers, be helpful in highlighting the distinct character of money market funds relative to other competing investments?*

   Rating symbols that distinguish the investment as a money market fund relative to other investments is helpful as it highlights that differentiating characteristics have been taken into consideration in determining the rating.

   Investors want to be able to compare the credit risk of investing in a single name instrument as compared to a fund even though they do have different characteristics. We agree that distinct rating symbols for money market funds ensure Treasurers recognise these as having different risk characteristics to those of other products. From a practical perspective some Treasurers would not find distinct rating symbols as helpful as they make comparison to other short dated investments that much harder. However we note that for comparative purposed you believe money market funds rated MF1 or MF1+ would exhibit a risk profile broadly consistent with Prime-1 rated investments, and MF2 and MF3 consistent with Prime-2 and Prime-3 respectively.

   Money market funds have now been defined by the SEC, IMMFA and CESR (the CESR has split definitions for short-term MMF and MMF). There may be situations where a fund falls within the risk profiles of Moody's MMF criteria but falls outside the definitions of the SEC, IMMFA and/or the CESR. In the reports provided alongside a fund rating it would be useful to highlight compliance with these definitions and also non-compliance stating the reason why.

4. *Can investment managers and other fiduciaries accommodate the proposed rating within their existing investment guidelines? If not, would the anticipated utility of the ratings lead managers to seek revisions to those investment guidelines to better accommodate the ratings?*

   The ACT is unable to comment from the investment manager's perspective as our members mainly work in non-financial companies. Within individual companies and groups and within any pension funds they run we imagine that changing mandates and investment policies should not be difficult. A good period of notice prior to withdrawing the existing ratings scale would be appreciated.

TREASURY, RISK AND FINANCE PROFESSIONALS
ACT

The Association of Corporate Treasurers

The ACT is the international body for finance professionals working in treasury, risk and corporate finance. Through the ACT we come together as practitioners, technical experts and educators in a range of disciplines that underpin the financial security and prosperity of an organisation.

The ACT defines and promotes best practice in treasury and makes representations to government, regulators and standard setters.

We are also the world's leading examining body for international treasury, providing the widest scope of benchmark qualifications and continuing development through training, conferences and publications, including *The Treasurer* magazine and the annual *Treasurer's Handbook*, and online.

Our 4,000 members work widely in companies of all sizes through industry, commerce professional service firms.

Further information is available on our website (below).

Our policy with regards to policy and technical matters is available at http://www.treasurers.org/technical/manifesto

Contacts: John Grout, Policy and Technical Director (020 7847 2575; jgrout@treasurers.org) Martin O'Donovan, Assistant Director, Policy and Technical (020 7847 2577; modonovan@treasurers.org) Michelle Price, Technical Officer (020 7847 2540 mprice@treasurers.org)	The Association of Corporate Treasurers 51 Moorgate London EC2R 6BH, UK Telephone: 020 7847 2540 Fax: 020 7374 8744 Website: http://www.treasurers.org