

INVESTMENT PERSPECTIVES

Prime MMFs are catching investors' interest again

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What this means to investors:

Prime money market fund (MMF) yields have become attractive versus other asset classes.

Investors have shown confidence again in floating net asset values (NAVs) and high liquidity levels.

The largest prime MMFs have been gaining assets, including the Wells Fargo Heritage Money Market Fund.



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What's attracting investors to prime MMFs?

A notable change has occurred within the MMF space. Prime MMFs have been attracting assets, as shown in Figure 1. This is a reversal of the exodus of money that these funds experienced leading up to the implementation of SEC Rule 2a-7 changes in October 2016.

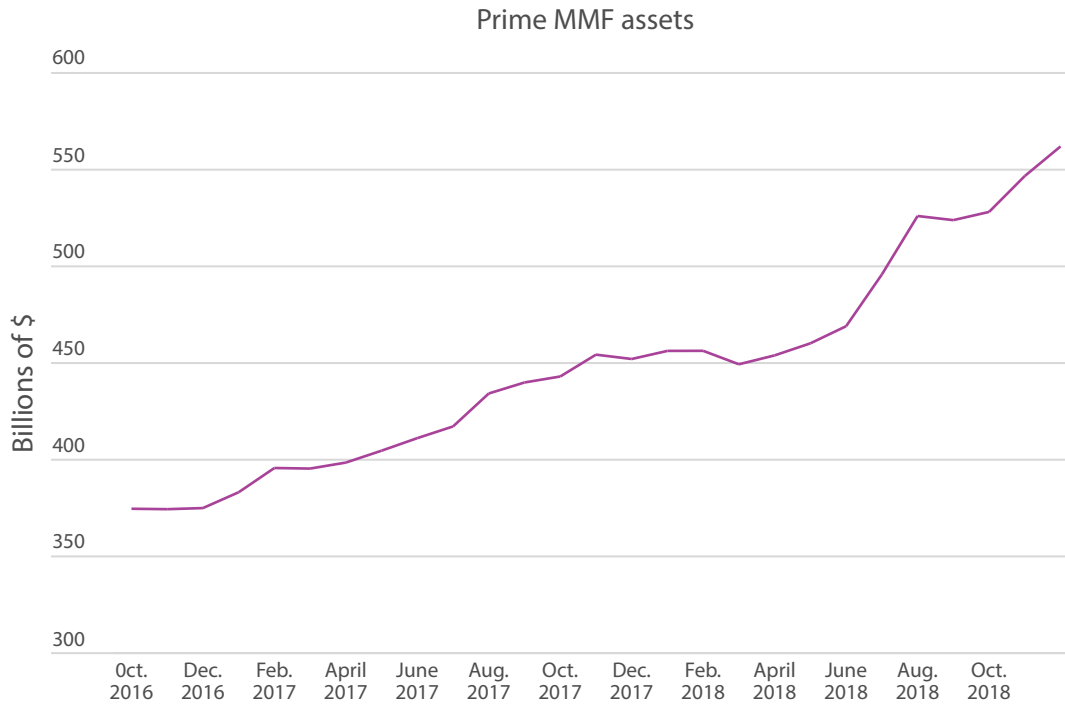
Prime MMF yields have become attractive compared with other asset classes. As the Federal Open Market Committee (FOMC) continues to remove its monetary policy accommodating, yields on prime MMFs have outpaced government MMF yields, thereby having created a wider yield differential. At the same time, prime MMFs have experienced minimal NAV movement, consistently high liquidity, and greater diversity of holdings within the funds. As a result, investors have become more comfortable with the operational aspects of prime MMFs.

The stringent liquidity, maturity, and diversification requirements mandated by the most recent SEC rules have led to a more stable product, especially in terms of liquidity and minimal NAV fluctuations. At Wells Fargo, these rules are consistent with the conservative manner in which the Heritage Money Market Fund has always been managed, emphasizing preservation of capital and high levels of liquidity.

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Figure 1: Investors have been putting money back into Prime MMFs

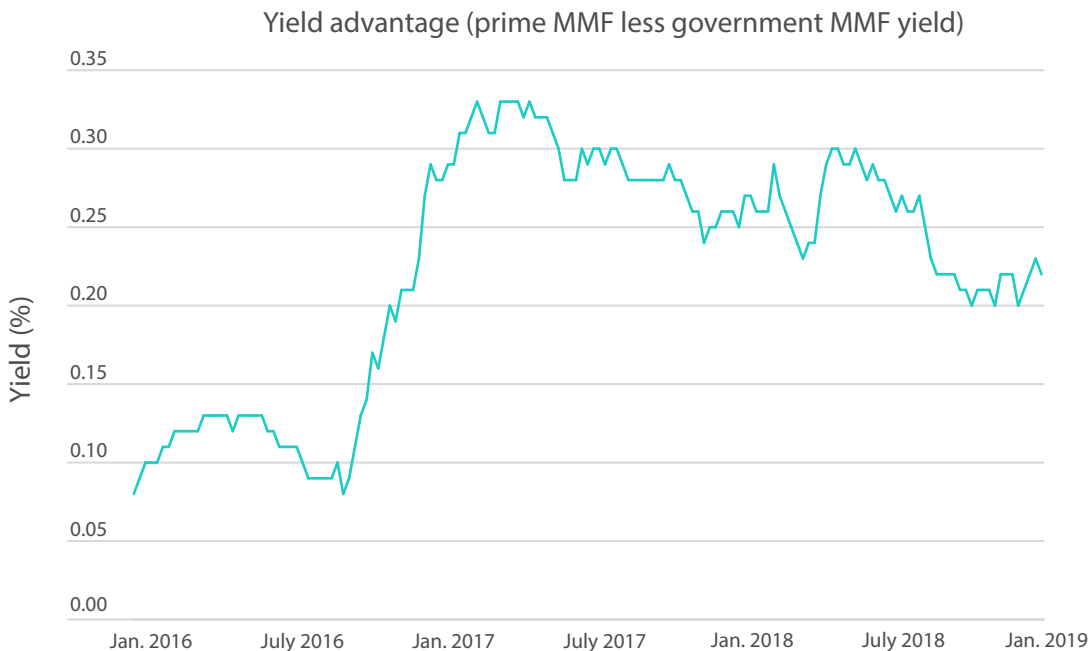


Source: iMoneyNet

Prime MMF yields are competitive

The yield advantage presented by prime MMFs has given investors an economic incentive to invest in these funds. In contrast to when the new SEC rules were enacted, monetary policy is no longer as accommodative. Back in 2016, the federal funds target rate was near 0%. Given the uncertainty about the effect of the new SEC rules, it was reasonable for cash investors to move to government MMFs because the yield differential was minimal. As the FOMC raised its target rate, though, the spread between the yields on prime and government MMFs widened. This yield advantage has given investors a reason to reexamine these funds.

Figure 2: Prime MMFs have seen a jump in their yield advantage over government MMFs



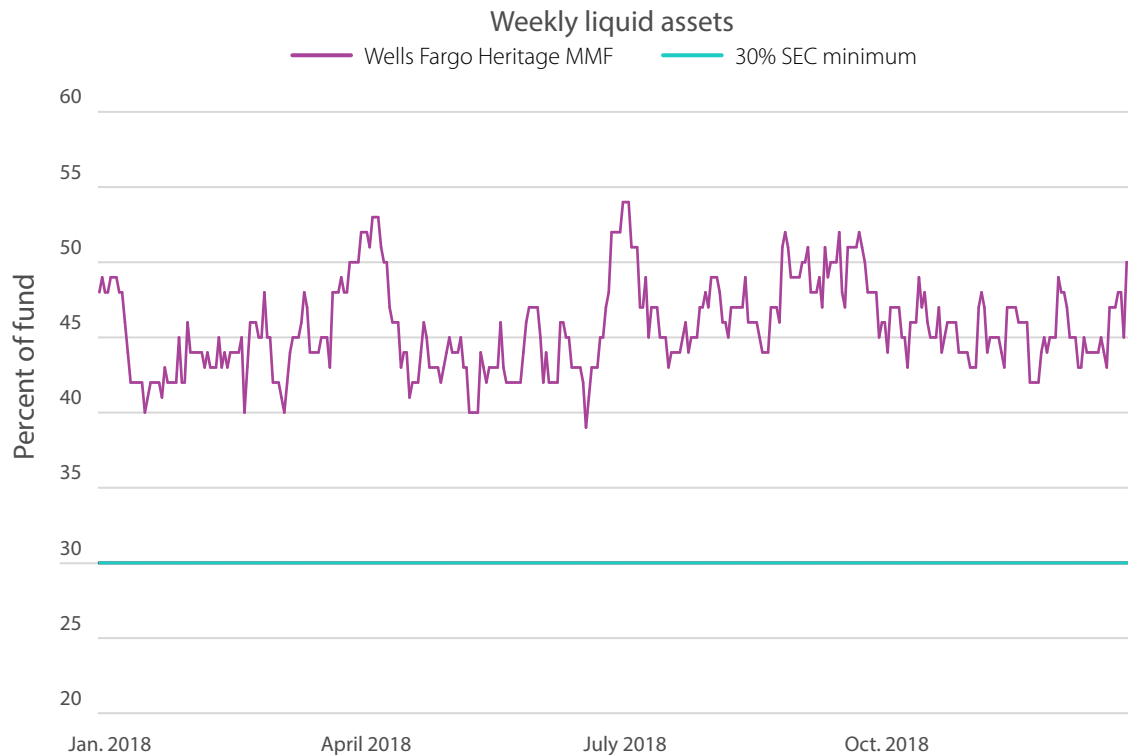
Source: iMoneyNet

Prime MMFs are highly liquid

One of the biggest concerns investors had about the 2016 SEC rules was the potential loss of liquidity from the imposition of fees and gates. To recap, the rules give fund boards the ability to impose a liquidity fee or redemption gate if a fund's weekly liquidity level drops below 30%. Investors appear to have become more comfortable with the idea of fees and gates now that they have had an extended period to observe weekly liquidity levels in prime MMFs. Fund managers have typically maintained weekly liquid asset levels well above the 30% threshold. The industry has done this, in part, to avoid triggering this event.

At Wells Fargo Asset Management, we've consistently maintained substantial liquidity well in excess of the 30% threshold in our flagship prime MMF, the Wells Fargo Heritage Money Market Fund. We believe the most important aspect of liquidity management is understanding the liquidity needs of the different investors in the fund. We have established know-your-customer procedures that allow for ongoing and regular communication between the sales and investment teams. As a result, the portfolio management team is better able to understand the nature and timing of the fund's cash flows and manage the fund's liquidity accordingly.

Figure 3. Weekly liquidity levels have been well above the 30% threshold



Source: Wells Fargo Asset Management as of December 31, 2018

Prime MMF floating NAVs have been remarkably stable

Another aspect of investing in a prime MMF is operational efficiency of the product. This type of fund still has the ability to provide same-day liquidity and still is reportable as cash. However, the adoption of a floating NAV was a significant concern for investors who were uncertain how much fluctuation they would see in their daily principal balance. We now have two years of empirical evidence that shows institutional prime MMF NAV fluctuations have been minimal.

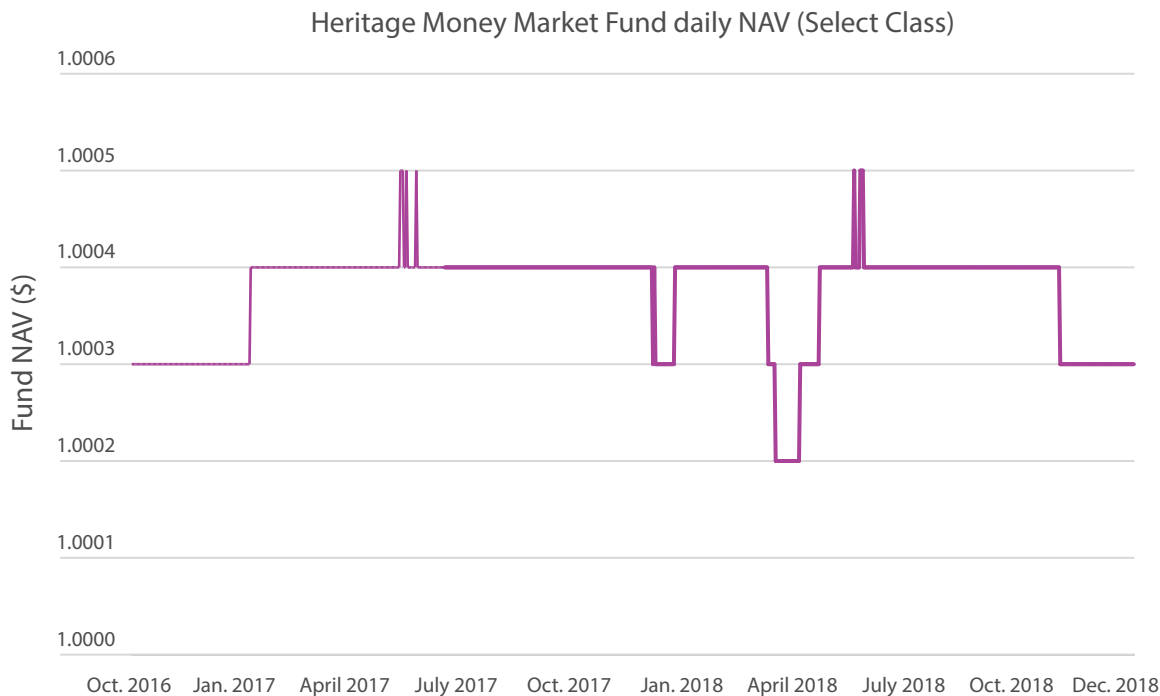
As evidence, iMoneyNet shows that the floating NAV of institutional prime MMFs, on average across the industry, changed 50 times between October 2016 and December 2018 with an average range of \$0.0005. During that same period, the Wells Fargo Heritage Money Market Fund (Select Class) had even lower volatility, with only 20 changes in its floating NAV across a range of \$0.0003. In percentage terms, the Heritage Money Market Fund was more than 50% less volatile than the industry average.

Figure 4. The Wells Fargo Heritage Money Market Fund NAV changes have been less volatile than the industry average

	Wells Fargo Heritage MMF Select Class	Industry average of prime institutional MMFs
Number of NAV changes	20	50
Range of NAV changes	\$0.0003	\$0.0005

Source: iMoneyNet

Figure 5. The Wells Fargo Heritage Money Market Fund NAV changes have been modest



Source: Wells Fargo Asset Management as of December 31, 2018

Portfolio composition offers attractive risk/reward proposition

We've already noted that prime MMFs now have a yield advantage despite being managed with a high degree of liquidity and minimal NAV movement. It's worth remembering that a number of other aspects of an actively managed prime MMF may benefit investors.

Diversification. MMFs are subject to diversification requirements under SEC Rule 2a-7. They invest in a wide range of issuers and money market sectors with limited exposure to any single issuer.

Credit risk management. We have a dedicated credit team that reviews each issuer to help ensure minimal credit risk is maintained. Our proprietary credit process and portfolio management tools used in concert can help us fine-tune the credit profiles of the fund and adjust it as conditions warrant.

Risk oversight. Stress testing a MMF's ability to withstand certain hypothetical market stress events is an important tool used by portfolio managers. These hypothetical events include increases in short-term interest rates, a downgrade or default of portfolio security positions, and a correlated increase in the credit spreads for certain portfolio securities, in combination with increases in shareholder redemptions. Results of these tests can help portfolio managers better manage risks in the portfolio and inform their investment decisions.

We expect the trend into prime MMFs is likely to continue

Because preservation of principal and daily liquidity have remained the most important aspects of prime MMFs, we believe investors will continue to reposition into them. Cash investors may be aided in their decisions about where to invest their short-term cash by considering three factors related to prime MMFs: the volatility of a fund's NAV, its liquidity level, and the size of the fund.

Investors reexamining prime MMFs now have two years of empirical data to review since the 2016 SEC rules were implemented. To recap, these rules included additional liquidity and diversification requirements as well as maturity restrictions. Investors may now see that the rules have made a difference in the construction of portfolios and, in response, liquidity levels have been consistently high and NAV volatility has been low even as the FOMC has continued to raise rates. In addition, prime MMFs still offer same-day liquidity and may be reported as cash.

Reasons to consider the Wells Fargo Heritage Money Market Fund

- **Lower NAV volatility**—half the volatility of the industry average
- **High levels of liquidity**—weekly liquidity in excess of 30%
- **Scale to manage effectively**—one of the 10 largest institutional prime MMFs¹
- **Attractive yield**—competitive relative to other prime and government MMFs

1. iMoneyNet; number 9 of 10 largest prime MMFs as of October 31, 2018

For more information

Please contact our Institutional Sales Desk at 1-888-253-6584. Or, visit our website at wellsfargo.com (Click *Institutional Cash Management*).

- For more information about various aspects of the SEC's new rules for MMFs, see the Money Market Fund Regulatory Resource Center within the Institutional Cash Management website.
- In addition, a total return calculator is available on our website to help investors understand how the yield and NAV movement of floating NAV MMFs versus stable NAV MMFs could affect returns.

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Diversification does not ensure or guarantee better performance and cannot eliminate the risk of investment losses.

Carefully consider a fund's investment objectives, risks, charges, and expenses before investing. For a current prospectus and, if available, a summary prospectus, containing this and other information, visit wellsfargofunds.com. Read it carefully before investing.

For floating NAV money market funds: You could lose money by investing in the fund. Because the share price of the fund will fluctuate, when you sell your shares they may be worth more or less than what you originally paid for them. The fund may impose a fee upon sale of your shares or may temporarily suspend your ability to sell shares if the fund's liquidity falls below required minimums because of market conditions or other factors. An investment in the fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. The fund's sponsor has no legal obligation to provide financial support to the fund, and you should not expect that the sponsor will provide financial support to the fund at any time.

For government money market funds: You could lose money by investing in the fund. Although the fund seeks to preserve the value of your investment at \$1.00 per share, it cannot guarantee it will do so. An investment in the fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. The fund's sponsor has no legal obligation to provide financial support to the fund, and you should not expect that the sponsor will provide financial support to the fund at any time.

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