Aviva Investors is the global asset management business of Aviva plc. The business delivers investment management solutions, services and client-driven performance to clients worldwide. Aviva Investors operates in 14 countries in Asia Pacific, Europe, North America and the United Kingdom with assets under management of £366 billion as of 31 December 2020. Aviva Investors welcomes the opportunity to respond to the FSB's consultation report on policy proposals intended to enhance Money Market Fund (MMF) resilience.

Overall

1. **What are the key vulnerabilities that MMF reforms should address? What characteristics and functions of the MMFs in your jurisdiction should be the focal point for reforms?**

In respect of the specific functioning of MMFs, there are a small number of areas we feel could benefit from reform to further enhance the resilience of the sector and we outline these further below. In addition, and in consideration of the policy reforms options being considered for the MMF sector, we would encourage regulators to consider overall market liquidity during the period of March/April 2020, and not just the response of the MMF sector. European MMFs demonstrated resilience; they continued to meet investors need for cash, and did not have to suspend or activate gates, despite the liquidity crisis. Reform should not concentrate solely on MMFs but also on the short-term funding market weaknesses.

Link between weekly and daily liquidity and fees and gates

- The link between weekly and daily liquidity and fees and gates is of most concern as this means that short liquidity, which is crucial for meeting redemptions cannot be used. Investors in MMFs track daily and weekly liquidity due to their association with fees and gates. Whilst the weekly liquidity thresholds were required as part of the MMF Regulation to enable MMFs to meet redemptions in times of stress, the COVID pandemic showed that this didn't actually happen. Instead, some MMFs sold assets at stressed levels, to prevent the liquidity buffers from going below their thresholds, and to prevent a further run on the funds as investors in MMFs withdrew their investment due to a threat of fees and gates.

Short-term market funding (STMF)

- As the report outlines, policy options aimed at MMFs themselves will not likely solve the structural fragilities in short-term funding markets (STFMs). Authorities might therefore consider adopting measures to improve the functioning of Commercial Paper (CP) and Certificate of Deposit (CD) markets.
- The crisis of 2020 was a completely global and unique situation, unlike anything seen in modern times. The market reaction and stresses seen in the market were only one part of the stress felt globally. It was also not a credit issue but rather a global sell-off issue which prompted redemptions from funds, demonstrating that this was not investors acting on the concern the funds might be downgraded.

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- Banking regulation exacerbated the problem as the market pressure happened at quarter end when balance sheets are at their tightest. Money market instruments, although short and highly rated are considered Level 2 and receive a haircut in High Quality Liquid Assets (HQLA) for Liquidity Coverage Ratio (LCR) calculations for banks.

- The illiquidity in the market in March 2020 resulted in the absence of a buyer of last resort, without central banks, due to balance sheet constraints of the banks. The US Federal Reserve's program was more extensive than that of the ECB, providing lending facilities for dealers purchasing assets from MMFs, the "Money Market Mutual Fund Liquidity Facility" (MMLF) and purchases of money market instruments via the "Commercial Paper Funding Facility".

2. What policy options would be most effective in enhancing the resilience of MMFs, both within individual jurisdictions and globally, and in minimising the need for extraordinary official sector interventions in the future?

CNAV/LVNAV concept

- We consider that moving away from the concept of constant and low volatility NAV and making funds free floating would be the most effective policy option. From our experience during the crisis, there were still some bids for commercial paper, but the prices were very unattractive.

- A variable NAV fund would be better placed to be able to accept those prices, sell the stock and move on. The real concern here is the treatment of such a fund with regards to cash and cash equivalence.

- In the US and some European countries there has been clear guidance on this, and the funds can be treated as cash equivalent. If this was more standardised globally, it would help to resolve this particular uncertainty.

Regulatory liquidity thresholds, fees and/or gates

- Delinking would allow buffers to operate countercyclically by enabling fund managers to use them to meet redemptions during times of stress. We expand on this further in response to question 3 below.

Anti-Dilution Levy

- We would support the ability to impose an anti-dilution levy in times of stress, to remove first mover advantage for redemptions.

Global co-ordination

- It is common practice that stress tests should not look at events in isolation but should instead combine events to come up with a complete view. We would encourage efforts towards a more consistent and coordinated responses from policy makers for global issues.

3. How can the use of MMFs by investors for cash management purposes be reconciled with liquidity strains in underlying markets during times of stress?

- The EU MMFR introduced prescribed limits for daily and weekly liquidity to ensure funds were able to meet redemptions in times of market stress. The linking of this to gates and fees meant the minimum requirements became an unintended red flag to investors making this liquidity bucket unusable. The threat to investors of fees and gates led to a flight of money from US Prime MMFs to US Government MMFs.
- It is our view that if you were to allow liquidity buffers to be used without a threat of fees or gates; without a breach of regulation, enabling MMFs to use their liquidity buffers to meet redemptions during times of stress, then this would make them safer during periods when liquidity is tight. It would mean the use of the funds by investors for cash management purposes would have no real impact during times of market stress.

Forms, functions and roles of MMFs

4. Does the report accurately describe the ways in which MMFs are structured, their functions for investors and borrowers, and their role in short-term funding markets across jurisdictions? Are there other aspects that the report has not considered?

- The report accurately describes the way MMFs are structured, their functions and roles. However, as referenced in our comments under the 'Overall' section, reform should not concentrate solely on MMFs but also on short-term funding market weaknesses. European MMF demonstrated resilience during Q1/Q2 2020; they continued to meet investors need for cash, and did not have to suspend or activate gates, despite the liquidity crisis.
- This was not a credit issue but a global sell-off issue which prompted redemptions from funds, demonstrating that this was not investors acting on the concern the funds might be downgraded. The liquidity issue captured all assets actively traded in the markets, even the most liquid government assets. We would encourage regulators to consider overall market liquidity during the period of March/April 2020, and not just the response of the MMF sector.
- MMF reforms, post the 2008 financial crisis, came into effect relatively recently and wholesale reform of these rules would not appear to be merited the response of the MMF sector to the 2020 crisis.

5. Does the report accurately describe potential MMF substitutes from the perspective of both investors and borrowers? To what extent do these substitutes differ for public debt and non-public debt MMFs? Are there other issues to consider?

- Smaller investors would be particularly disadvantaged if there were no money market funds. They would not be able to access the market or assess credit quality and would be open to misjudging risk and have an over reliance on credit rating agencies. As an example, UK local authorities suffered in the Global Financial Crisis (GFC) when the Icelandic banks failed, because the risks had not been properly understood.
- The only viable alternative is bank deposits which, for a number of reasons, including banking regulation and excess liquidity in the system, are undesirable to the banks themselves, and who are, in many cases, actively discouraging them.
- Short-term bond funds are not a viable place to invest large amounts of liquid cash as they would not be able to cope with large scale redemptions and they don't carry the amount of liquidity MMFs do. The likely outcome is that we would see funds gated regularly and investors defaulting as they were unable to access their cash.

Vulnerabilities in MMFs

6. Does the report appropriately describe the most important MMF vulnerabilities, based on experiences in 2008 and 2020? Are there other vulnerabilities to note in your jurisdiction?

- It is a fair reflection of the experience of some money fund providers but not all.
- During the March 2020 crisis there would have still been the same liquidity strains in the STFM even without money funds. Direct holders of CDs and CP would still have struggled to sell them. T-Bills as well as Sovereigns, Supranational and Agencies (SSA's) were also volatile and illiquid during this period despite the fact that they are meant to be the risk-free assets. This demonstrates that this issue wasn't just confined to credit and further highlights the lack of secondary market.
- The liquidity issue captured all assets actively traded in the markets, even the most liquid government assets. Therefore, this was not a short-term funding market issue, but a widespread liquidity crisis.
- It should be noted that the largest cumulative outflow during the crisis was 30% (for rated LVNAV funds). Therefore, weekly liquid assets for LVNAV funds would have been able to meet those redemptions without the need for forced selling. The cash that was withdrawn from the funds would have needed to be invested elsewhere i.e., deposited with banks overnight so bank funding should not have been impacted.
- It is our view that the MMFR was operating as it should do, and that the liquidity was still ultimately available within the system.
- The US Federal Reserve's program was more extensive than that of the ECB, in providing liquidity to the market. The EU and Bank of England did not seem to have the same concerns with market liquidity. They were prepared to provide funding to the corporate borrowers and banks but did not provide support to the money market funds.

Policy proposals to enhance MMF resilience

7. Does the report appropriately categorise the main mechanisms to enhance MMF resilience? Are there other possible mechanisms to consider? Should these mechanisms apply to all types of MMFs?

- The report seems to capture a comprehensive range of options and includes the options considered in the recent ESMA consultation.

- We are of the opinion that a number of the options would be likely to result in fund providers withdrawing from the market, because they would make the funds either uneconomic to manage, or unattractive to investors. We outline these issues below:

- **Swing pricing** would make the ability to pay same day operationally very difficult and would in our view turn investors away. The swing pricing mechanism is very difficult to implement in a thinly traded market.
- **Minimum balance at risk** (MBR) is more equitable but there may be difficulties determining what the MBR is. We doubt that it would be adequate in times of stress. There would also be the requirement for daily changes to clients MBR as they added and redeemed from the fund.
- **Capital buffers** would risk driving out all but bank sponsored providers so would therefore increase the concentration risk of the industry to only a handful of funds. This is potentially even more destabilising.

8. Does the assessment framework cover all relevant aspects of the impact of MMF policy reforms on fund investors, managers/sponsors, and underlying markets? Are there other aspects to consider?

- The framework does appear to cover all aspects; however, we feel that the likelihood of investors moving into alternatives is overplayed. As previously said the current market and regulatory conditions mean banks will not accept large tranches of cash or will impart punitive charges on holdings.
- Short-term bond funds would be less liquid and more likely to gate.
- Investing directly would only be open to larger investors and they would not be in a position to match the credit work that the funds do, therefore increasing the reliance on rating agencies and the chances of making mistakes, such as investing in Icelandic banks in the lead up to the GFC.
- The focus is on MMFs and not the underlying short-term market disfunction.
- There is a need for a more coordinated action when there is a global market disruption.

9. Are the representative policy options appropriate and sufficient to address MMF vulnerabilities? Which of these options (if any) have broad applicability across jurisdictions? Which of these options are most appropriate for public debt and non-public debt MMFs? Are there other policy options that should be included as representative options (in addition to or instead of the current ones)?

- We support de-coupling regulatory liquidity thresholds; they have made the extra liquidity on the funds both a risk comparison metric for investors and a minimum threshold for the manager to manage the fund to.
- Liquidity buffers were already sufficient to meet redemptions. We consider that MMFR achieved the objective of making the system more robust, but funds need to be able to freely access the liquidity without fear of penalty.
- The introduction of an Anti-dilution levy and the move to free floating NAV would be sufficient to make the system more robust. The VNAVs do not have the same fees and gates issue so they are able to use the cash buffers to meet redemptions, as was the case in 2020.
- Obligations that require capital to be put aside would lead to fund closures and further concentration of the market. Moving the funds away from same day access would make them unusable by investors so would potentially mean the death of these funds. It should be noted that it wouldn't have mattered whether funds were T+0, T+1 or T+2 settlement; as liquidity in the market was non-existent, funds would still have used their short cash to meet redemptions.
- The option for public debt funds in most jurisdictions is not viable due to a lack of available assets.

10. Does the summary assessment of each representative option adequately highlight the main resilience benefits, impact on MMFs and the overall financial system, and operational considerations? Are there any other (e.g., jurisdiction-specific) factors that could determine the effectiveness of these options?

- Broadly speaking, we consider it to be an adequate assessment.
- In respect of eligible asset limits and limiting MMFs to Government MMFs, there are some specific issues such as supply, liquidity and ability to sell being limited due to minimum requirements. There is also a question around a central authority's ability to buy back their own paper.

11. Is the description of variants and the comparison of their main similarities/differences vis-à-vis the representative options appropriate? Are there other variants to consider?

- Yes, we consider the description of variants to be appropriate and we do not believe there are other variants to consider.

12. Are measures to enhance risk identification and monitoring by authorities and market participants appropriate complements to MMF policies? Which of these measures are likely to be most effective and why? Are there other measures to consider?

- We do not consider that there is a need for additional stress testing. There are already adequate requirements under MMFR for stress testing the portfolios. In addition, all rated funds are stress tested daily against the rating agency's criteria.
- Market data is not easily determined in the money markets due to issues with transparency. We would be supportive of efforts to provide for better pre and post trade data in STFM. We are aware of a number of commercial initiatives, and the ECB STEP label, which are helping to consolidate data.

Considerations in selecting policies

13. Are the key considerations in the selection of policies to enhance MMF resilience appropriate? Are there other considerations that should be mentioned?

- Capital requirements would cut the number of participants to bank sponsored funds which would narrow the number of participants and increase the risk in the market.
- Investors in funds need them to be cash or cash equivalent so the operational side of the fund, same day settlement and capital preservation are paramount. In March 2020 it wouldn't have mattered if the funds seeing outflows were T+0, T+1 or T+10, there were no buyers at prices palatable to the funds.
- Underlying market disfunctions need to be addressed.

14. Which options complement each other well and could potentially be combined? What are the most appropriate combinations to address MMF vulnerabilities in your jurisdiction? Which combinations are most effective for different MMF types and their functions?

- Remove the link between liquidity and fees and gates.
- Allow for anti-dilution levies.
- Abolish LVNAV and CNAVs but retain their level of liquidity for VNAV funds.

15. To what extent should authorities seek to align MMF reforms across jurisdictions? Is there a minimum set of policies or level of MMF resilience that should be considered at the international level to avoid fragmentation and regulatory arbitrage?

- Keeping regulation broadly in line across jurisdictions is the most optimal response. However, it is recognised that markets in different currencies have their own characteristics so some consideration should be made about their behaviours. For example, the US Government fund market can accommodate size given the depth of the T-Bill market but for GBP the market is very much smaller and more limited so would not be able to accommodate huge demand for UK T-Bills.

- We encourage policy makers to coordinate responses as far as possible in order to avoid regulatory arbitrage. There is a lack of harmonisation and transparency across markets. National regulators were not always consistent in their responses, there was a lack of clarity in terms of the legal frameworks and what each central bank could buy. We consider that better coordination and greater consistency between regulators in different jurisdictions would be a positive enhancement going forward.

Short-term funding markets (STFMs)

16. Does the report accurately describe problems in the structure and functioning of STFMs and how these have interacted with MMFs in stress periods?

- Liquidity for CDs and CP in normal markets is generally fine, and we have not experienced problems selling when required.
- Proposals to improve market functioning would be welcome. The Federal Reserve allowing funds to sell to them worked well for the US market. The mere presence of a scheme in Europe and UK would aid liquidity and give participants more confidence in the liquidity of the assets even if it was never used.

17. What other measures should be considered to enhance the overall resilience of STFMs? How would those measures interact with MMF policy reforms and how effective are they likely to be in preserving market functioning in stress times?

- Back stop schemes from central banks would provide extra confidence for market participants to buy secondary paper, even in markets short of liquidity. The biggest problem in March 2020 was funds with cash were not buying for fear of having to sell even if it turned out they didn't need to.
- Considering short-term paper as HQLA would make it more desirable and improve liquidity.
- Making CD's and CP repo-able into central banks would make them more desirable to banks.
- Generally, make the assets more desirable for banks to own, would improve liquidity.

18. Are there any other issues that should be considered to enhance MMF resilience

- None that have not been covered already.