EUROPEAN MONEY MARKET FUND REGULATION: A PROVEN AND SOUND FRAMEWORK

Introduction

France is one of the three main European centers for the domiciliation and management of money market funds[1]. Money markets are an important short-term capital market that contributes to the financing of the economy. As such, they are one of the pillars of the global financial system. Money market funds play an important role in this market, allowing the encounter between a short-term financing need and a short term investment, offering a remuneration in line with money markets. In France, they allow for more than 40 years (since 1981) a sustainable financing of the short end of the economy, exclusively via a variable net asset value structure.

AFG, as representative of the main domiciliation and management center of EUR denominated money market funds[2], strongly believes that the European Money Market Fund Regulation (Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds "MMFR") proved to be a very well-balanced piece of regulation and cannot be modified without posing unnecessary risks at a time when savings and investments are incentivized in Europe.

All graphics are coming from the following ESMA's report : 2023 ESMA's report.

MMFR has proven its efficiency

The existing MMFR already imposes rigorous management rules on both asset and liabilities of money market funds through compliance of liquidity ratios (daily and weekly), adapted to the various types of money market funds ("Low-volatility net asset value", "Public debt constant net asset value", and "Variable net asset value"). The existing liquidity ratios have proven their accurate calibration during the COVID-19 crisis as no major incidents were observed despite extremely challenging conditions, notably regarding underlying markets' liquidity.

The stress on the markets triggered by the COVID-19 crisis revealed that money markets funds were resilient and able to keep on functioning during this unprecedented crisis. Indeed, unlike the great crisis of 2008, money market funds met the massive redemptions they recorded. It is also noteworthy to recall that outflows were only driven by the dash-for-cash crisis whereby a huge number of economic actors had to face a sudden drop in their revenues. In no way redemptions were caused by a distrust of investors towards money market funds. Otherwise, money market funds would not have recorded a spectacular bounce in inflows, as early as May 2020. Moreover, the other events / crises that followed the COVID-19 crisis, such as the war in Ukraine, the hyperinflation that followed it, the exceptional turnaround in monetary policy - which triggered a rapid rise in interest rates of 450 basis points -, and the bankruptcies of Credit Suisse and some US regional banks in 2023, demonstrated again and again the resilience of EU-domiciled money market funds.

[1] France domiciliates 430 Bn EUR worth of money market funds as of end of March 2025.
[2] As of ESMA's Market Report on EU MMF market 2023: "The share of MMF by domicile and currency indicates that France accounts for 62% of EUR MMF assets"

Money market funds are key for the financing of the European economy.

As described in the last 2023 MMF report by ESMA[3], EUR denominated money market funds account for 45% of total money market funds assets (EUR 653bn). Most of them are Variable Net Asset Value funds – "VNAVs" (roughly 80%). Consequently, VNAs) represent the bulk of the short-term debt denominated in Euro.

They invest massively in commercial papers (CPs) and other short-term bank securities. They represent a structural source of financing for key real economy actors such as banks, insurance companies, agencies, and industrial corporates. Raising liquidity ratios would be detrimental to this capacity for financing European issuers with a maturity longer than one week.

GRAPH 1. Maturity profile for government debt.
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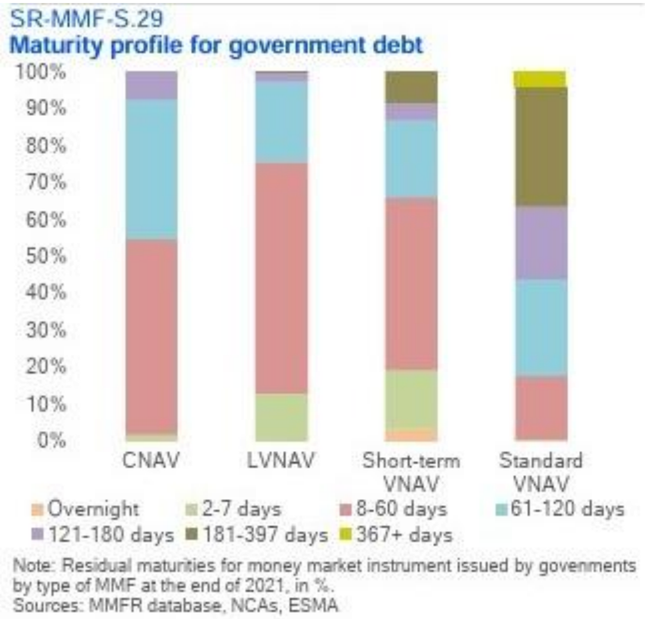
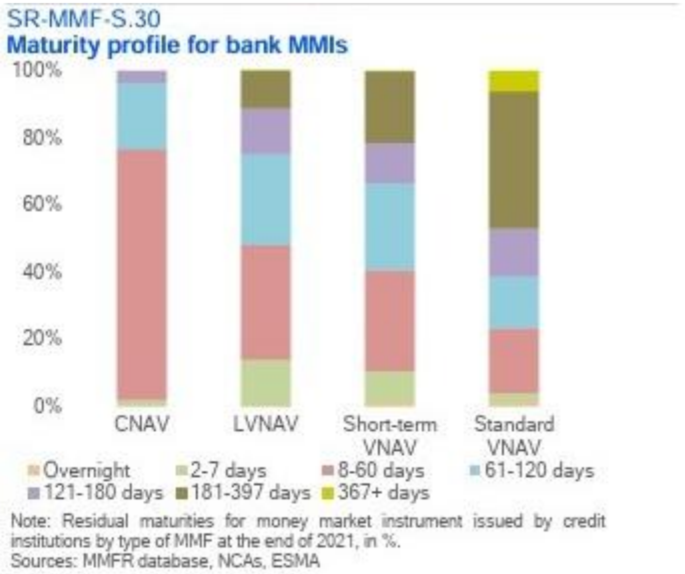


Source: ESMA.

GRAPH 2. Maturity profile for bank money market instruments



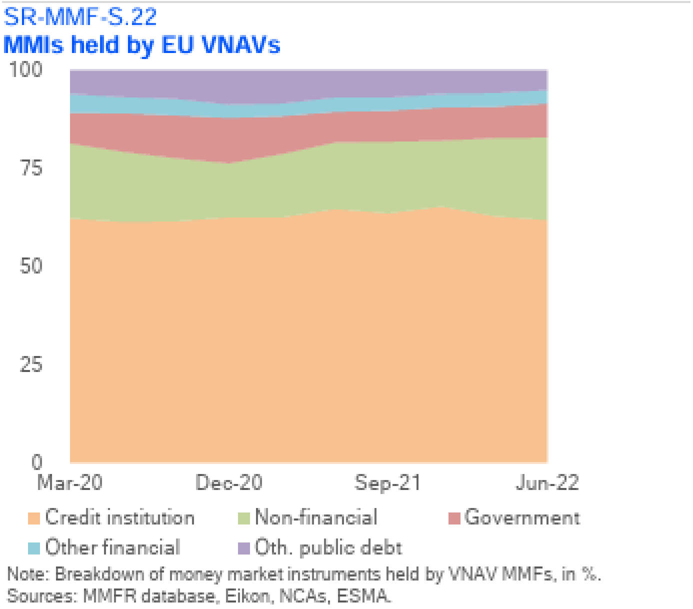
Source: ESMA.

VNAV funds offer subscriptions and redemptions permanently made at the market price.

VNAV funds invest in a well-diversified portfolio of short-term assets valued at market prices offering full transparency to market evolutions. This diversification applies both to instruments and issuers and leads to a very low risk efficient portfolio, with a controlled idiosyncratic risk of a single issuer or an instrument type. On their liability side, the investors' base is diversified and subject to permanent monitoring for liquidity risk management purposes.

[3]. ESMA50-165-2391 ESMA Market Report on EU MMF market 2023

GRAPH 3. Money market instruments held by EU "Variable Net Asset Value" money market funds



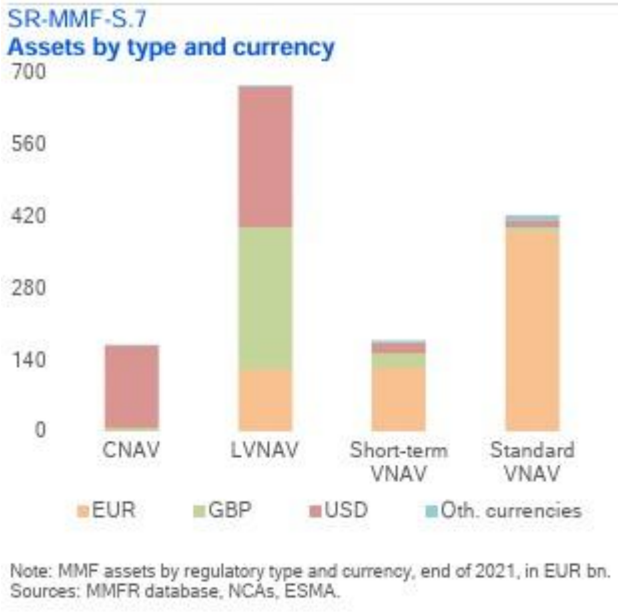
Source: ESMA.

Most stakeholders share the view that the COVID-19 crisis shed light on the temporary and sudden dry-up of liquidity in short-term funding markets (STFMs). There is a need to encourage regulators are to primarily focus on taking steps to improve STFMs functioning and favor more harmonization, standardization and transparency. AFG believes that the proper functioning of the market for bank commercial papers is essential to ensure a minimum level of liquidity and more transparency under market stress:

- The activity in the short-term banking securities market during times of crisis is a crucial source of liquidity, enabling the fulfillment of redemption requests. Therefore, it would be worth exploring the incentives that could allow banks to play a stabilizing role, in cases of liquidity stress in the markets, by repurchasing their own paper (and possibly those issued by other banks).
- Unlike bond or equity markets, most STFMs' activity takes place in the primary issuance market and during stressed times, all players are placed in the same direction which gives the secondary market a "binary" aspect. Obviously, new players should be able to step into these markets. Liquidity should first be improved to attract them and then make this market enter a virtuous circle.

Moreover, by definition, money market funds denominated in non-EU currencies are less likely to finance the EU economy.

GRAPH 4. Money market funds' assets by type and currency.



Source: ESMA.

In addition, liquidity risk management of money market funds has recently been strengthened

The Money Market Fund Regulation is indirectly amended via the UCITS and AIFM Directives' recent revision meant to further strengthen the liquidity risk management framework through the introduction of liquidity management tools. Hence, all money market funds will be equipped with at least one liquidity management tool by April 2026. This will strengthen further their autonomy and resilience in case of stress of market liquidity. It appears both reasonable and necessary that any review be paused until these tools enter into application and their effects can be assessed.