Consumer Education Media Release
Association for Savings and Investment South Africa (ASISA)
16 July 2009

Pick your money market fund with confidence

Many investors who thought they had safely parked their money in a money market fund were horrified when recent newspaper articles questioned the safety of these investment instruments.

Money market fund investors were left wondering whether their money was really parked in a money market fund or whether they had been misled by the name of the fund and had unintentionally channeled their money into a more risky fund. And questions raised about the liquidity of these funds also had investors spooked.

Peter Dempsey, deputy CEO of the Association for Savings and Investment South Africa (ASISA), says by asking the right questions and by doing a bit of research investors will quickly establish whether their money is invested in a true money market fund that is regulated and therefore offers legal protection.

But first, says Dempsey, it is very important that you understand that a money market unit trust fund is not the same as a savings account or a money market account offered by a bank.

What is a money market fund?

A money market fund is a unit trust fund and not a bank savings or investment account. As with all unit trust funds, money invested in a money market fund is pooled with that of other investors.

In the case of a money market fund the fund manager uses the invested money to buy money market paper and very short-term bonds issued by a variety of institutions that want to borrow money.

Dempsey says most investors do not investigate the underlying instruments held by money market funds, because understanding money market instruments is not easy.

“However, if you really had to delve deep into the holdings of the various funds, you would find that the assets in money market fund portfolios are mainly spread across the biggest banking institutions in the country, providing you with the added protection that comes with diversification.”

A money market account on the other hand only invests in the instruments issued by one bank and it is treated as a bank account. Unlike the assets in a money market unit trust fund, the assets of a money market account form part of the balance sheet of that bank.

Dempsey explains that by law, the assets of a unit trust fund may not form part of the balance sheet of the asset manager or the registered management company. To make sure that investors’ assets are not affected should the asset management company run into trouble, the assets of a unit trust fund have to be held in trust by appointed trustees.

When you invest in a money market fund you buy units, generally at 100c (R1) per unit. Unlike other unit trust funds, money market funds keep the unit price stable at 100c per unit.

However, says Dempsey, it is possible for a money market fund to make a loss.

He says while this has never happened in South Africa, should a money market fund make a loss, your number of units held in the fund would be reduced, but the 100c unit price would be retained.

"It has happened, however, that a local money market fund was exposed to securities that delivered a 0% return," says Dempsey. "In this case investors did not suffer a capital loss, but the interest they earned on their investment dipped."

Dempsey says with very few exceptions, local money market funds have proven to be well managed and stable investments over the years. He explains that money market funds are obliged to invest in line with strict legal requirements that aim to minimize the exposure by these funds to risky money market securities. Money market securities include banker's acceptances, commercial paper, negotiable certificates of deposit and government bills.

What legal protection do you enjoy?

All unit trust funds are regulated by the Collective Investment Schemes Control Act (Cisca). In terms of regulations to the Act, the exposure to different types of investments as well as to individual banks and investment companies is limited. The following rules apply to money market funds:

- The assets of money market funds may not be invested in money market securities with a maturity of more than 12 months.
- The average maturity of securities held by the fund as a whole may not exceed 90 days.
- In addition, fund mangers are restricted in terms of how much money they loan to institutions.

Dempsey explains that the short-term nature of the assets held in a money market portfolio significantly reduced the risk of the fund. However, he adds, money market funds do not offer guarantees.

Am I invested in a money market unit trust fund?

The easiest way to determine whether you are invested in a true money market unit trust fund is by consulting one of the following:

- The ASISA website (go to www.asisa.co.za and click on the *Info Centre* tab and select *Collective Investment Schemes*)
- The Financial Services Board (FSB) website (go to www.fsb.co.za and click on the *CIS* tab and select *Local CIS* under *List of Approved Schemes*)
- The unit trust pricing section of financial newspapers (not all newspapers carry the money market fund prices as they generally remain at 100c).

The ASISA website lists all approved collective investment schemes, including money market unit trust funds, as per their respective categories. This makes it easier to find the fund you are looking for. If you are interested in a money market fund or already invested in one, make sure it appears in the Money Market category.

Peace of mind checklist:

Dempsey advises that for your own peace of mind you obtain answers to the following questions when investing in a money market fund:

- Am I looking at a money market unit trust fund or a money market account offered by a bank?
- Do I know and trust the company offering the fund? Does the asset management company managing the fund have a good track record overall?
- Ask your adviser whether he has investigated the strength of the asset manager's compliance department and whether he has ensured that the systems deployed are adequate when it comes

to measuring compliance by fund managers? The compliance department is key in making sure that fund managers stick to the rules. Asset management companies provide interested advisers with access to this information.

- Also ask your adviser about the team managing fixed interest portfolios such as the money market fund. The bigger the team the less the risk of one person breaching or bending the rules.
- What is the average maturity of securities held by the fund? The closer this average is to 90 days, the higher the liquidity risk of the fund. The liquidity risk defines the ability of a fund to pay out your money as soon as you require it. However, the average maturity level of a money market portfolio changes frequently and is not a guarantee of liquidity.
- How soon will my money be in my bank account once I disinvest? While most funds aim to pay within 24 hours, the fund's collective investment scheme deed may stipulate 15 working days. This means that if several investors disinvest substantial amounts at the same time, the fund manager may delay payment by 15 working days.
- If you are really risk averse, you could restrict yourself to money market funds that are given a rating based on the quality of the underlying instruments by rating agencies such as Moody's, Fitch or S&P. However, most funds are not rated. This is because a rated fund may not exceed an average maturity of 45 days, which reduces the potential for higher returns. In addition, the rating also does not present a guarantee of the fund's stability or liquidity; it simply indicates that it has met the standards for its rating.

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ASISA represents the majority of South Africa's asset managers, collective investment scheme management companies, linked investment service providers, multi-managers, and life insurance companies. ASISA was formed in 2008 by members of the Association of Collective Investments (ACI), the Investment Management Association of South Africa (IMASA), the Linked Investment Service Providers Association (LISPA) and the Life Offices' Association (LOA).