Cash management market update

BlackRock.

April 6, 2020

Getting better over time

- Over the past week, BlackRock saw continued strong flows into government money market funds (MMFs), a material slowing in the rate of outflows from prime MMFs, and further signs of improved functioning at the front-end of the credit markets.
- Activity in the Money Market Mutual Fund Liquidity Facility (MMLF) — a source of liquidity the Federal Reserve (Fed) established to serve as a backstop for prime and municipal MMFs — rose to approximately $53 billion last week through Wednesday, April 1, according to the Fed. In our view, confidence that supplemental liquidity can be accessed when needed has prompted a timely increase in market activity in the credit space. We anticipate further normalization of market conditions as the entire range of recently announced Fed programs becomes fully operational.
- The Fed's reverse repurchase agreement program (RRP) has lately served as an important outlet for investable cash from eligible MMFs, providing a "non-negative" interest rate of 0%. Daily take-up recently rose to its highest level since 2017, peaking around $285 billion on the last day of the quarter.
- As further evidence, in our opinion, that the Fed will continue to do what it takes to support normal market functioning, modifications were made to a regulatory restriction known as the Supplementary Leverage Ratio (SLR). Specifically, Treasuries and deposits are now temporarily excluded from this calculation for large banks. We expect this will free up space on balance sheets and improve liquidity conditions in the broader Treasury market in the very near future as this policy change was made effective immediately.
- The net new supply of Treasury bills (T-bills) in the past week surpassed expectations, increasing by $319 billion, with multiple cash management bills comprising a large percentage of the total issuance. This additional volume contributed to a modest increase in T-bill rates, which provided a small, but welcomed amount of relief following part of the T-bill curve's recent foray into negative territory. In our view, the expected $1 trillion increase in net T-bill supply over the next two quarters should continue to lend a degree of support to rates as well.
- The 3-month Libor-Overnight Indexed Swap (OIS) spread — a gauge of stress in the financial system – crested around 1.38% in the week before dropping to 1.32% on Friday. The forward market reflects expectations for a steady and sizeable contraction in this measure in the months ahead.
- In the municipal market, excess inventory of variable rate demand notes (VRDNs) continued dropping during the week to around $2.8 billion on Friday, down approximately $4.5 billion from last week, and well off the $31 billion high set earlier in March. In response, the Securities Industry and Financial Markets Association Index (SIFMA) Index of 7-day VRDNs fell nearly 300 basis points from the prior week to close at 1.83%. We view this movement as a positive indicator that the municipal cash market is stabilizing.
- If you are interested in learning more about BlackRock's global economic outlook and perspective on COVID-19, please view our Investment Institute's commentary here.
- To read more on the Fed programs mentioned above, please see our Insights on www.blackrock.com/cash.

The opinions expressed are as of April 6, 2020 and are subject to change at any time due to changes in market or economic conditions.
Sources Federal Open Market Committee, Bloomberg, the Federal Reserve.

Money market fund positioning

Government & Treasury funds

The funds shifted their positioning slightly from the week prior to capitalize on some new market opportunities. The aforementioned new supply in T-bills and cash management bills allowed our portfolio managers to avail themselves of slightly improved yields.

Thankfully, the T-bills that were trading with negative yields the past two weeks are now trading above 0.00% in the secondary market. This can be attributed in part to the liquidity the Fed has supplied recently, along with the month-end and quarter-end dynamics, as constrained dealer balance sheets have resulted in supply that is healthier and cheaper.

Across the platform, there was a higher allocation to T-bills compared to last week. For the applicable funds, the shift to T-bills was made from certain repurchase agreement (repo) and agency allocations to seek a yield advantage. Current repo rates had been yielding on average 0.01%, and the influx of supply in Treasuries had made this asset class relatively more attractive to comparable agency investments, in our opinion.

The new opportunities that were presented this week resulted in slightly longer weighted average maturity (WAM) and weighted average life (WAL), which are shown below.

	WAM	WAL	Weekly Liquidity
BlackRock Liquidity Funds FedFund	35	103	64%
BlackRock Liquidity Funds T-Fund	38	95	100%
BlackRock Liquidity Funds Federal Trust Fund	56	103	73%
BlackRock Liquidity Funds Treasury Trust Fund	55	94	100%

Source: BlackRock. As of April 3, 2020.

Prime funds

Investors in prime MMFs are seeing the benefits of the Fed facilities and the adjustment made to the SLR in the form of much-needed additional liquidity on bank balance sheets.

The mark-to-market (MTM) NAVs of prime MMFs have come off their lows and climbed each day during the past week – evidence in our opinion of a more fluid state of liquidity and calmer markets. (See below for the current MTM NAVs.) While across the industry prime MMF outflows have slowed, this category of funds has seen a 28% decrease in assets year to date through March 31 (source: iMoneyNet). However, in a welcome reversal, certain BlackRock prime MMFs saw net inflows in the past week.

As investors gain confidence in the stability of markets, our prime MMFs remain active by continuing to predominantly roll overnight exposures in commercial paper and bank deposits while opportunistically adding select commercial paper in longer tenors such as 3-months. We expect that these exposures will aid the funds' yields.

Portfolio WAMs are currently targeted in the thirty-day range. As market volatility persists, we seek to position the funds' durations with a focus on liquidity and principal preservation.

	MTM NAV	WAM	WAL	Weekly Liquidity
BlackRock Liquidity Funds TempFund	$1.0004	31	79	44%
BlackRock Liquidity Funds TempCash	$1.0005	38	86	41%
BlackRock Money Market Portfolio	$1.0003	48	65	47%
BlackRock Liquid Environmentally Aware Fund (LEAF®)	$1.0002	43	83	43%

Source: BlackRock. As of April 3, 2020.

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Past performance is not indicative of future results.

Municipal funds

Within the municipal space, we continued to see a sharp decline in the supply of VRDN inventory last week. Due to the attractive yield levels on these securities, many different investors including bond funds, separately managed accounts, and taxable crossover buyers bought up the inventory leading into March month-end. Adding to the current high level of VRDN demand from these non-traditional investors, many municipal MMFs continued to prefer buying VRDNs over longer-dated commercial paper or municipal notes in order to maintain a defensive posture. As the SIFMA index represents the average yield on weekly VRDNs, these dynamics caused its reset lower to 1.83% by end of week. Currently, VRDN inventory on dealer balance sheets stands below historical averages and remains at a very manageable level, which we believe will continue to exert a downward bias on VRDN yields in the near future.

In typical years, April represents a period of seasonally high VRDN supply as investors redeem from municipal MMFs in order to pay for tax liabilities. Given the extension date for tax payments until July, however, we expect the typical seasonal pattern to be less pronounced this month as the redemption curve is likely flattened this year.

We are continuing to seek to position our municipal MMFs with high levels of daily and weekly liquidity by maintaining an overweight to VRDNs and other par put securities while remaining selective on commercial paper extension trades with 30- to 90- day tenors. Our portfolio WAMs remain conservatively positioned.

	WAM	WAL	Weekly Liquidity
BlackRock Liquidity Funds MuniFund	22	22	71%
BlackRock Liquidity Funds MuniCash	16	16	83%
BlackRock Liquidity Funds California Money Fund	6	6	96%
BlackRock Liquidity Funds New York Money Fund	6	6	98%

Source: BlackRock. As of April 2, 2020.

Ultra-short bond funds

The introduction of the Fed's MMLF improved liquidity conditions in the tier 1 commercial paper and certificates of deposit market. This has led to moderate tightening in Libor-OIS spreads, although they remain widened.

Front end corporate bond spreads continue to tighten following the Fed's announcement of the corporate credit facilities for both the primary and secondary markets. The recent modest tightening in these spreads and better liquidity conditions have improved the mark-to market pricing of the securities in the funds thereby increasing the funds' net asset values per share.

We continue to focus on liquidity by purchasing very short-dated high-quality commercial paper and opportunistically adding exposure to floating rate notes indexed to 3-month Libor as these spreads have been favorable. We continue to maintain a neutral duration and believe the short term credit markets will see increased spread tightening and improved liquidity when the Fed's corporate credit facilities become fully operational.

BlackRock Global Cash Management is committed to keeping investors informed, especially during times of market uncertainty. Please contact your relationship manager with any further questions or check blackrock.com/cash for updates.

Want to know more?

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