



## Money Market Funds

### Request for Comments

#### Scope of the Criteria

Lianhe Ratings Global Limited ("Lianhe Global") applies the money market fund ("MMF") criteria to MMFs and similar investment vehicles that mainly invest in short-term fixed income instruments and their primary objectives are to preserve principal and provide liquidity to investors. Short-term fixed income instruments are typically high-quality debt securities with maturities of less than a year, providing income in the form of interest payments or purchased at a discount to par.

Lianhe Global invites market participants to provide comments and feedback on this proposed criteria by 31 January, 2024 by submitting their comments and feedback to [info@lhratingsglobal.com](mailto:info@lhratingsglobal.com).

The criteria does not represent a comprehensive coverage but only addresses key rating factors to form our credit opinions and will be reviewed periodically.

#### Overview

Lianhe Global has developed the rating framework for MMFs based on our rating knowledge and experience. The criteria do not represent a comprehensive coverage but only address key rating factors which we consider are important for accessing MMFs' ability in preserving principal and providing liquidity. The MMF industry is continuously evolving and the rating framework or some rating elements of these criteria may not adequately address the emerging risk characteristics. Lianhe Global continues to look at the MMF industry development and may revise the criteria when we deem it necessary.

In addition, the criteria do not include non-market event risk as these events are usually unforeseeable in nature and are unlikely to be considered when assigning MMF ratings. Similarly, extreme tail-risk scenarios may not be incorporated. Also, Lianhe Global relies on the fund or fund administrator to provide data and may not always be able to identify data errors; this may have an impact on rating assignments.

Lianhe Global conducts regular surveillance on our assigned MMF ratings, and requests data from rated MMFs on a monthly basis generally. Lianhe Global may seek information at any time or on a more frequent basis in the event of heightened credit and/or liquidity stress, or any event risk. Apart from the data provided by the rated MMFs, Lianhe Global also review other relevant public and non-public available information.

#### Money Market Fund Rating Symbols and Definitions

A MMF rating is an opinion on the relative ability of a MMF or similar investment vehicle to provide liquidity and preserve principal in the MMF's target investment markets by limiting credit, liquidity, and market risks. We add the suffix "mf" to the six rating categories (AAA, AA, A, BBB, B, and C) to differentiate MMF ratings from Lianhe Global's Long-term Issuer Credit Ratings. MMF ratings are not and should not be construed as an investment recommendation.

Rating	Definition
AAA <sub>mf</sub>	Money market funds have fairly strong ability to provide liquidity and preserve principal

#### Analysts

Joyce Huang, CFA

+852 3462 9586

[joyce.huang@lhratingsglobal.com](mailto:joyce.huang@lhratingsglobal.com)

Toni Ho, CFA, FRM

+852 3462 9578

[toni.ho@lhratingsglobal.com](mailto:toni.ho@lhratingsglobal.com)

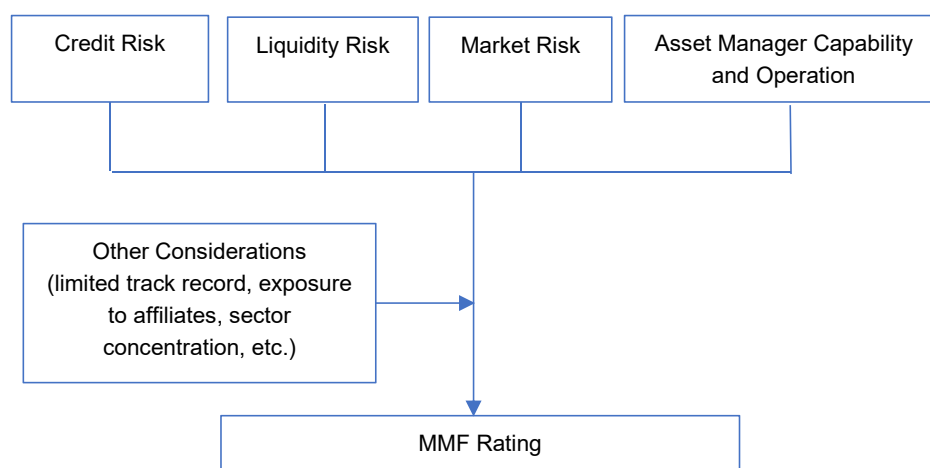
Rating	Definition
AAmf	Money market funds have strong ability to provide liquidity and preserve principal
Amf	Money market funds have moderate ability to provide liquidity and preserve principal
BBBmf	Money market funds have marginal ability to provide liquidity and preserve principal
Bmf	Money market funds have weak ability to provide liquidity and preserve principal
Cmf	Money market funds are unable to provide liquidity or preserve principal

## Rating Framework and Key Factors

The following diagram shows Lianhe Global's general approach in deriving our opinions of the investment quality of MMFs or similar investment vehicles. We use a combination of qualitative and quantitative analysis to assess four key factors: credit, liquidity, and market risks, and asset manager capability and operation, and may incorporate other considerations (where applicable) in the final assessment.

Other considerations that may affect our rating opinions include the legal, regulatory and/or operating environment, limited track record, exposure to affiliates, sector concentration, indirect investments to a portfolio of securities (e.g. third-party MMFs and asset-backed securities), and stress tests. Lianhe Global may assign MMF ratings to MMFs with no or limited track record, such as newly launched funds or funds with short operating history. In these cases, Lianhe Global mainly focuses on the MMF's stated investment guidelines, the fund manager's track record and experience in fund management, as well as the MMF's model portfolio in assessing the MMF rating.

**The rating framework for money market funds:**



Primary Factor	Sub Factor
Credit Risk	Credit Quality Concentration

Primary Factor	Sub Factor
	Asset Maturity
Liquidity Risk	Portfolio Liquidity
	Redemption Risk
Market Risk	Sensitivity to Market Movements
	Portfolio Pricing and Other Risks
Asset Manager Capability and Operation	Sponsor's Financial Strength
	Manager's Competent and Record
	Management Framework and Control

### Credit Risk

Credit risk refers to the risk and loss caused by a default of the debtor and/or a decrease in price of the investment in the portfolio. Generally, short-dated and highly-rated investments, together with a diversified investment portfolio tend to have lower credit risk and higher ability in preserving principal of a MMF. Lianhe Global assesses the exposure to credit risk of a MMF by investigating the credit quality, concentration, and asset maturity of the investment portfolio.

### Portfolio Credit Quality

When analysing the credit quality of a MMF, we mainly look at the international credit ratings of the individual securities and/or the issuers of these securities invested by the MMF and evaluates the asset-weighted average credit quality of the investment portfolio. Generally, the higher the credit ratings of the securities invested by a MMF, the lower the credit risk of the MMF and the lower possibility of credit loss suffered by its investors. In the absence of a public rating, Lianhe Global may refer to our private rating or internal assessment in the credit analysis. Other mitigating factors will also be considered, such as short tenor, the manager's ability to limit credit loss, seniority of instruments, secured exposure, and guarantee.

### Portfolio Concentration

Generally, a highly concentrated investment portfolio would make it difficult to diversify its credit risk effectively. Consequently, the investment portfolio may suffer significant loss if a credit event occurs. A high concentration risk would usually occur if the investment portfolio excessively concentrates on securities issued by a single issuer or bank deposits of an individual bank. We may view investments in securities issued by related entities whose creditworthiness is highly correlated as an exposure to a single issuer.

Lianhe Global examines a MMF's management of concentration risk by investigating its exposure to a specific investment or issuer compared to its total asset value. Other factors or exceptions would be considered or allowed, such as strong credit quality assets, strongly collateralized exposures, and highly liquid or short tenor assets.

### Asset Maturity

Limiting maturities of portfolio securities can reduce uncertainties and mitigate credit risk of a MMF. Lianhe Global examines the maturities of all securities in the portfolio and consider that the maturities should be less than or equal to 397 days for AAAMf-AAmf rated funds, or up to 2 years for Amf-BBBmf rated funds. Exception is allowed for securities with certain conditions, such as floating rates, strong credit quality, and strong market liquidity.

	<b>AAAmf</b>	<b>AAmf</b>	<b>Amf</b>
<b>Credit Quality</b>	Asset-weighted average credit quality equivalent to a high-investment-grade international rating of BBB+ or above, or with other mitigating factors	Asset-weighted average credit quality equivalent to an investment-grade international rating of BBB or above, or with other mitigating factors	Asset-weighted average credit quality equivalent to an investment-grade international rating of BBB- or above, or with other mitigating factors
<b>Concentration</b>	Concentration risk is well managed. Any single exposure should be ≤ 10% of total asset value; exception is allowed for strong credit quality assets, strongly collateralized exposures, highly liquid/short tenor (≤ 60 days) assets, etc.	Concentration risk is well managed. Any single exposure should be ≤ 10% of total asset value; exception is allowed for strong credit quality assets, strongly collateralized exposures, highly liquid/short tenor (≤ 90 days) assets, etc.	Concentration risk is adequately managed. Any single exposure should be ≤ 10% of total asset value; exception is allowed for good credit quality assets, adequately collateralized exposures, adequately liquid/short tenor (≤ 180 days) assets, etc.
<b>Asset Maturity</b>	Maturities of all securities should be ≤ 397 days for AAAmf-AAmf rated funds or ≤ 2 years for Amf-BBBmf rated funds. Exception is allowed for securities with floating rates, strong credit quality, strong market liquidity, etc.		

## Liquidity Risk

A MMF should be able to meet its investors' redemption requests in full and on time, including at times of market stress or sudden and large fund outflows. Accordingly, Lianhe Global examines a MMF's liquidity risk by investigating its portfolio liquidity (including available daily and weekly liquidity, and illiquid long-dated assets), and redemption risk.

### Portfolio Liquidity

#### *Available Daily and Weekly Liquidity*

Lianhe Global examines the proportion of available daily and weekly liquid assets to the total asset value of a MMF's investment portfolio. Eligible assets for daily liquidity include cash, overnight maturing securities, and highly liquid assets available for timely redemptions/disposals. Eligible assets for weekly liquidity include securities maturing within 7 days, in addition to eligible daily liquid assets.

Other mitigating factors are considered when assessing a MMF's liquidity risk, such as committed liquidity facility, repurchase funding agreements, other liquidity sources, and highly stable/predictable liquidity needs.

#### *Illiquid Long-dated Assets*

Significant illiquid long-dated assets may have a negative impact on a MMF's liquidity profile assessment as the higher the proportion of illiquid assets and/or restricted assets, the lower the liquidity level of the investment portfolio.

### Redemption Risk

Lianhe Global identifies a MMF with high redemption risk under certain circumstances, including a concentrated investor base, volatile fund flow history, and stressed market liquidity. A MMF subject to high redemption risk may need to maintain additional liquidity to achieve a certain rating level.

	<b>AAAmf</b>	<b>AAmf</b>	<b>Amf</b>
<b>Available Daily Liquidity</b>	≥ 10% of total asset value, or with other mitigating factors	≥ 10% of total asset value, or with other mitigating factors	≥ 5% of total asset value, or with other mitigating factors
<b>Available Weekly Liquidity</b>	≥ 25% of total asset value, or with other mitigating factors	≥ 15% of total asset value, or with other mitigating factors	≥ 10% of total asset value, or with other mitigating factors

### Market Risk

Market risk refers to adverse market movement which would negatively affect the market value and/or cause a loss of a MMF's investment portfolio. For instance, an unfavourable change in interest rates may cause a drop in the market value of the investment portfolio. Lianhe Global assesses the market risk of a MMF through examining its portfolio sensitivity to market movements, portfolio pricing deviations and other risks.

### Portfolio Sensitivity to Market Movements

Weighted average maturity ("WAM") and weighted average life ("WAL") are the two main metrics Lianhe Global uses in assessing the sensitivity of a MMF to market movements. WAM is used to measure the sensitivity of a MMF to changes in market interest rates, while WAL is used to measure the sensitivity of a MMF to changes in credit spreads.

#### *Weighted Average Maturity*

WAM is calculated as the asset-weighted average days to the next reset date for floating-rate instruments or the maturity date for fixed-rate instruments.

#### *Weighted Average Life*

WAL is calculated as the asset-weighted average days to final maturity after considerations of any optional extensions.

### Portfolio Pricing and Other Risks

#### *Portfolio Pricing*

Managers should have robust policies and procedures with respect to marking the managed investment portfolios to market on a regular basis. Significant deviation of portfolio pricing from actual values may have a negative impact on the market risk assessment of a MMF.

#### *Currency Risk*

Assets in a MMF's investment portfolio should be denominated in the base currency or fully hedged. Currency risk would be material if the assets are not denominated in the base currency or fully hedged, which may have a negative impact on the market risk assessment of the MMF.

## *Derivatives*

Derivatives (if employed) should be only for hedging purposes. Using derivatives for non-hedging purposes may have a negative impact on the market risk assessment of a MMF.

	<b>AAAmf</b>	<b>AAmf</b>	<b>Amf</b>
<b>Weighted Average Maturity</b>	≤ 60 days	≤ 90 days	≤ 180 days
<b>Weighted Average Life</b>	≤ 120 days	≤ 180 days	≤ 240 days

## **Asset Manager Capability and Operation**

Lianhe Global generally conducts a qualitative assessment of the capability and competent of the fund sponsor and asset manager when assigning MMF ratings. The sponsor and manager should have sufficient resources, competent, and expertise to manage the fund. Management framework should be well structured with established policies and procedures in place in managing credit, market, and liquidity risk, and prudent internal control.

### **Sponsor's Financial Strength, Manager's Competent and Record**

#### *Sponsor's Financial Strength*

A sponsor with weak financial strength (equivalent to a below-investment-grade international credit rating) may have a negative impact on the MMF rating.

#### *Manager's Competent and Record*

An asset manager with weak competent of managing investment portfolio or with a volatile/poor track record may have a negative impact on the MMF rating.

### **Management Framework and Control**

#### *Management Framework and Control*

Insufficient/inadequate investment infrastructure, policies, and procedures with respect to credit, market, and liquidity risk management may have a negative impact on the MMF rating.

#### *Counterparty Risk*

Counterparties in all transactions should have sound financial strength (equivalent to an investment-grade international credit rating), or may have a negative impact on the MMF rating.

#### *Custodian Bank*

A custodian bank with weak financial strength (equivalent to a below-investment-grade international credit rating) or with weak ability/operational framework for segregation and safekeeping of the MMF's assets may have a negative impact on the MMF rating.

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