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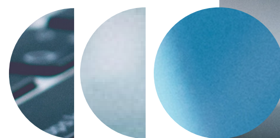
# Money market strategies: when cash is king

## 60 seconds with the portfolio manager



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**This marketing communication is intended for non-professional investors.**

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# 60 SECONDS WITH THE FUND MANAGER

**Money market strategies aim to offer a low-risk and liquid way for investors to generate higher returns than traditional savings accounts. Pierre Boyer, Elodie Brun, and Benjamin Schoofs, portfolio managers, share their insights on the asset class.**

## What do investors need to know about money market strategies?

A money market strategy invests in highly-liquid, short-term instruments, typically those maturing in less than 3 months. These include debt issued by financial and non-financial entities (corporates), sovereign governments and related agencies, as well as supranational bodies, among others. Investing in such instruments provides an essential source of financing for these entities, often complementing traditional bank loans, especially for non-financial companies.

Our strategies aim to deliver returns in excess of the euro short-term rate (€STR)(1) and to outperform traditional savings accounts. The European Securities and Markets Authority (ESMA) defines and regulates money market strategies, imposing rules on liquidity, the remaining life of eligible securities, interest rate duration (WAM) and credit sensitivity (WAL) at the portfolio level.

- WAL (Weighted Average Life) measures the average time left until the underlying securities in a strategy mature. It helps gauge credit sensitivity. The longer the reimbursement of the principal is postponed, the higher is the credit risk.

- WAM (Weighted Average Maturity) measures a portfolio's sensitivity to interest rate changes. Unlike WAL, WAM takes into account the interest reset dates for floating-rate securities. The more frequently the interest rate is reset, the less sensitive the strategy is to interest rate changes.

We manage our money market strategies conservatively. To further reduce volatility, we limit our WAM to 150 days (rather than the 180 of the ESMA's guidelines) and our WAL to 250 days (instead of 365)(2). In addition, we follow strict liquidity rules and maintain a strong focus on quality and diversification. Every issuer in our strategies benefits from a thorough internal fundamental analysis of its business, financials, cash flow generation, liquidity profile as well as incorporating our internal ESG profile and external analyses and ratings from agencies.

## Can money market strategies shake off their "boring" reputation?

With yields now firmly in positive territory, we've noticed that our enthusiasm is catching on. Clients are rediscovering the tactical value of maintaining liquidity in their portfolios, and recognising that liquidity does not have to be detrimental to total return.

In terms of day-to-day portfolio management, there is never a dull moment, especially given how active central banks have been over the past two years! In a nutshell, our return engine is driven by interest rate risk, credit risk and liquidity premia. These require strong convictions about the direction of rates, optimization of the yield curve, arbitrage

(1) This is an indicative data which may change overtime.
(2) This is an indicative data which may change overtime.

between floating or fixed-rate securities, and use of interest-rate swaps for additional flexibility. Common money market instruments include commercial paper, certificates of deposit, bank deposits, floating rate bonds, short term fixed bonds, and repurchase agreements.

Our investment universe is broad, covering most OECD countries. Although our strategies don't take active currency exposure and are fully hedged, we invest in developed market currencies to take advantage of cross-currency opportunities.

## Does it make sense to invest in money market strategies in today's environment?

Money market strategies currently[3] offer an attractive return, especially compared to the low rates offered by traditional bank deposits. In addition, their flexibility, liquidity and diversification also appeal to investors seeking a refuge without the potential return drag from holding cash in their portfolio.

Typically, low-risk investments generate lower returns, but in the current environment, money market strategies are offering higher short-term returns while maintaining low risk and low volatility. This is an excellent combination from a risk-adjusted point of view. With yield curves inverted due to investor expectations of a policy pivot, central banks remain cautious about easing their restrictive policies too soon or too fast. Money market yields closely follow actual nominal rates rather than anticipated policy changes, and our active approach to duration and credit risk management helps us maximize opportunities in the market.

We maintain a positive credit exposure in 2023 and slightly positive in 2024, favouring issuers with strong balance sheets. However, we remain cautious due to both our conservative approach, and because of ongoing uncertainties about economic growth, geopolitical tensions, and the potential end of central bank asset purchase programs (which could widen credit spreads). With respect to interest rates, our analysis shows that longer-term fixed rates already factor in significant rate cuts. We continue to favour a strategy with low interest rate duration, balancing floating-rate securities with short-term fixed-rate securities. This approach seeks to help our strategies deliver higher total returns with low volatility, while protecting against inflation surprises and shifting expectations for future rate cuts.

## Have liquidity and low volatility always been hallmarks of money market strategies?

Since the 2008 financial crisis, European money market strategies are better protected against systemic risks. In 2009, the European Commission introduced regulations to enhance investor protection and financial stability. These rules require money market strategies to invest in well-diversified, high-quality assets. Additionally, as an internal constraint, Candriam require strong ESG metrics. All these rules and constraints offering better protection than simple bank deposits These regulations also harmonize asset valuation standards and liquidity requirements to promote stability.

While liquidity can still be an issue in the weaker elements of the money market segments, we are reassured by the European Central Bank's strong commitment to financial stability, which acts as a backstop for the market. This commitment provides additional security for investors in money market strategies.

## How do you differentiate yourselves from competitors?

We set ourselves apart by combining disciplined risk management, active investment strategies, and a thorough process for selecting issuers:

- Tailored interest rate and credit exposure targets: every month, our committee carefully defines targets for interest rate and credit exposure, ensuring that our strategies are well-aligned with current market conditions.

- Active management on the yield curve: we focus on short- to medium-term opportunities within the yield curve, using active strategies to take advantage of market shifts while aiming for strong risk-adjusted returns. We also maintain a balance of different maturities to avoid overconcentration in any single area.

- Rigorous issuer selection: we apply strict quality filters and in-depth analysis to select issuers for our portfolios, ensuring they are financially sound and resilient. This includes a careful assessment of liquidity and setting strict maturity rules based on the issuer's credit rating and financial strength.

(3) In October 2024, the return on the money market strategy was between 3.25% and 3.35%. Source: Candriam.

- Disciplined risk management: our independent risk management team ensures that we strictly follow both internal and external risk guidelines, helping to protect our investors.

This approach has allowed us to avoid credit or liquidity issues, even during times of crisis. In other words, we maintain a competitive asset class with a constant focus on security and delivering consistent returns.

# The main risks of the strategy are:

**• Risk of capital loss:**

There is no guarantee for investors relating to the capital invested in the strategy in question, and investors may not receive back the full amount invested.

**• Interest rate risk:**

A change in interest rates, resulting in particular from inflation, may cause a risk of losses and reduce the performance of the strategy (especially in the event of a rate increase if the strategy has a positive rate sensitivity and in the event of a rate reduction if the strategy has a negative rate sensitivity). Long term bonds (and related derivatives) are more sensitive to interest rate variations. A change in inflation, in other words a general rise or fall in the cost of living, is one of the factors potentially affecting interest rates.

**• Sustainability risk:**

The sustainability risk refers to any environmental, social or governance-related event or situation that might affect the performance and/or reputation of issuers invested in.

Sustainability risks may be subdivided into three categories:

- Environmental: environmental events may create physical risks for the companies invested in.

- Social: refers to the risk factors linked to human capital, the supply chain and the way companies manage their impact on society.

- Governance: these aspects are linked to governance structures.

The sustainability risk may be specific to the issuer, depending on its activities and practices, but may also be due to external factors. If an unforeseen event occurs in a specific issuer such as a strike or more generally an environmental disaster, the event could have a negative impact on the performance. In addition, issuers which adapt their activities and/or policies may be less exposed to the sustainability risk.

**• Credit risk:**

Risk that an issuer or a counterparty will default. This risk includes the risk of changes in credit spreads and default risk. Some strategies may be exposed to the credit market and/or specific issuers in particular whose prices will change based on the expectations of the market as regards their ability to repay their debt. These strategies may also be exposed to the risk that a selected issuer will default, i.e. will be unable to honour its debt repayment, in the form of coupons and/or principal. Depending on whether the strategy is positively or negatively positioned on the credit market and/or some issuers in particular, an upward or downward movement respectively of the credit spreads, or a default, may negatively impact the performance. When evaluating the credit risk of a financial instrument, the Management Company will never rely solely on external ratings.

The risks listed are not exhaustive, and further details on risks are available in regulatory documents.

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