

# Money Market Insight™

Monthly money market industry analysis from the publisher of IBC's Money Fund Report™

## INSIDE THE INDUSTRY

### ◆ RECENT TURMOIL COULD SPARK "BIG BANG" IN ASIAN MONEY FUNDS

This month we discuss the parallels between today's embryonic Asian money fund industry and the U.S. money fund industry of 20 years ago. Similarities between the two periods include skyrocketing (and volatile) interest rates, massive losses in stocks and bonds, and a major flight from mutual funds. While currency considerations, specifically the flight to the dollar during the Asian crisis, could derail our theory, Asian specialists we spoke with have already seen an increase in interest and activity among Asian money funds. Money funds exist in one form or another in almost all of the more industrialized Asian countries, though the majority of funds are not fully "Rule 2a-7" compliant as of yet.

Though offshore funds have garnered a lot of attention recently, the growth has been equally impressive in foreign markets. In the past two years, India, South Africa, Malaysia and a number of other countries launched their first money funds. Many haven't imposed standards as strict as the U.S., but the strides have been impressive. Even China is expected to have money funds within the year. Of course, it hasn't exactly paid off if you're counting in dollars. But for domestic savers, of which there are plenty, these new money funds are giving the native banks a run for their money.

Pui-Wing Tam, in a recent *Asian Wall Street Journal* article, says, "The one reason to pick a regional currency fund would be if you already hold that currency and will need to use it in the near future: the interest earned in a money market fund could be substantial, as some countries in the region now have interest rates near 20%." The article also adds, "Hong Kong investors have also been flocking to HK dollar-denominated money market funds to take advantage of the higher interest rates."

### 20 Years Ago: Money Funds Save the U.S. Mutual Fund Industry

While some may not recall, during the 1970's the U.S. mutual fund industry was in dire straits. The bear market of the '70's was beginning to take its toll on fund assets. However, money market funds were there as the "safety net" to catch these assets before they left the complexes (and mutual funds) entirely. During the second oil price shock of 1979-80, when short-term interest rates shot up to 20 percent, money fund assets rose from \$10.4 to \$75.4 billion. In the following two years, total assets surged to \$207.8 billion. Neither bank products nor bonds could possibly adapt rapidly enough to the wildly fluctuating rates of this period.

John Hudson, senior partner at Hudson & Hudson Research in San Francisco, consultants specializing in global currencies and central banking, tells us, "By factor of elimination, yes, money is moving into money funds." He adds that some countries will benefit more than others. "Historically, when a country installs strong central bank independence, then it really does draw money. It stabilizes the currency.... A lot of the wealth that was destroyed was in fixed assets and in bad loans, so I think these markets are still in the embryonic stage," says Hudson.

On the other hand, some aren't sure that the smaller Asian countries, particularly the ones with the most volatile short-term rates, will see money move into money funds. "Our theory is that it holds true for developed countries," says Federated's Debbie Cunningham. She adds that money funds in Japan, due to their extremely low interest rates, will face a tough sell.

Of course, a significant obstacle to a booming money fund industry is the lack of a large, liquid domestic money market. This "Catch-22" scenario — money markets needing borrowers and borrowers needing supply — may delay the growth of funds in some nations, but development is already well under way in almost every single nation. The recent volatility alone should cause much of the financing in these countries to shift into the short-term market, adding volume to these money markets.

### MRFs (Money Reserve Funds) Ready to Launch in Japan

While Japan clearly doesn't have the interest rates to attract assets into money funds, the deregulation "Big Bang" should pave the way for a full scale fund industry in this nation in the coming months. Already, Fidelity, Merrill Lynch and others are preparing to offer funds, and we expect many other U.S. fund companies to follow.

Russ Long, a director at Standard & Poor's Managed Funds Ratings, says, "Japan has a fledgling money fund industry. They have new guidelines on what they call money reserve funds, MRFs, from their version of the ICI (the Investment Trust Association, ITA), which are very similar to Rule 2a-7. I believe Daiwa and Yamaichi [who is in talks with Merrill Lynch] have come out with the first two." (Current overseas yen funds have looser maturity guidelines.)

"Nomura is advertising that they'll be starting one in April.... They [Japanese SROs] basically copied 2a-7 — the maturity, pricing, quality, and ratings guidelines.... They're really just starting this, and they hope to be very successful," says Long. He adds, "All that money in those yen-denominated offshore funds — it's not there for the yield." •

### MONEY FUNDS UNDERGOING "BIG BANG" IN ASIA

Country	State of Industry	Assets (US \$) Est.	Recent S-T Rate	
Australia	Advanced	\$2 bil.	5.0%	Advanced: \$1.00 a share; Rule 2a-7-like regulation; mature money markets; 20+ funds.
China	Embryo	\$1 bil.	10.0	
Hong Kong	Intermed	\$3 bil.	9.0	Intermediate: Rule 2a-7-like regulation; liquid money markets; >10 funds.
India	Begin	\$500 mil.	12.0	
Indonesia	Embryo	\$50 mil.	37.0	Beginner: Developing regulation and money markets; 5-9 funds.
Japan	Intermed	\$50 bil.	3.0	
Malaysia	Embryo	\$50 mil.	11.0	Embryonic: Fewer than 5 funds; loose regulation; small money market.
New Zealand	Intermed	\$200 mil.	8.5	
Philippines	Embryo	\$50 mil.	16.9	
Singapore	Begin	\$100 mil.	5.6	
Taiwan	Begin	\$1 bil.	6.9	
Thailand	Embryo	\$50 mil.	17.0	

Rate Sources: Hudson & Hudson Research, Dow Jones, IBC Financial Data.



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