INVESTMENT OPERATIONS

BEYOND MONEY MARKET FUND REFORM: THE SHIFT TOWARDS INTRADAY VALUATIONS
By October 2016, the U.S. money market fund industry must comply with a range of new rules, as devised and voted in by the Securities and Exchange Commission (SEC). While practical challenges are undoubtedly in store, can reform also inspire long-term operational improvements?

Large money managers lead the ways

As they prepare to achieve compliance, U.S. money market funds, asset managers and third-party administrators (TPAs) already seem intent on not just meeting the requirements of regulation but actually exceeding them. Leading the way are the largest money market funds, in their aim to support the intraday valuation of prime portfolios.

According to the new regulations, prime institutional money market funds must now sell and redeem shares based on a floating net asset value (NAV), rather than the stable NAV they were allowed to maintain before. Unlike the floating NAV, however, the striking of multiple NAVs a day is not an explicitly stated requirement of the SEC. At best this remains a grey area: an implied expectation an implied expectation for funds to provide more than one distinct price a day per portfolio.

Regardless, the largest firms are looking to establish intraday valuation as part of their accounting and transfer agency regime. With smaller organizations bound to follow suit, the onus is on TPAs to support their clients’ intraday pricing ambitions with robust systems and processes.

In their eagerness to support intraday pricing, large money managers are doing more than establishing themselves as thought leaders and early adopters. Intraday pricing effectively equates to sharper risk management, making it easier to attribute an issue to an isolated group of transactions, rather than a whole day’s trading.

The intraday pricing challenge

It may not be a regulatory requirement in its own right, but intraday pricing is sure to become a key enabler of floating NAV adoption. At the same time, the need to strike multiple NAVs intraday creates a number of new pressures for money market fund operations. Transfer agents, for example, will need to report share transactions to the fund accountant multiple times on a daily basis, and there must be an ability to handle multiple money movements, too.

To better manage these challenges, money market funds, fund managers and TPAs will need to meet a number of key operational objectives:
Operational objective #1: provide a rapid, real-time flow of data

Real-time accounting and transfer agency systems are a prerequisite for efficient intraday valuation. In terms of transfer agency operations in particular, batch-based processing is still prevalent across the industry. Many transfer agents may use a shadow database to capture trade data, but this can never be as accurate or comprehensive as processing transactions in real time. What’s more, even if a transfer agency system can handle multiple valuations a day, it still relies on a real-time accounting system which can calculate several NAVs daily – and to four decimal points under the new regulation. With real-time data passing rapidly back and forth between the two systems, intraday pricing becomes a realistic and achievable objective.

Operational objective #2: support intraday price validation

In turn, transfer agency and accounting systems must be fed by reliable pricing data. For intraday valuation especially, organizations need fast, scalable, auditable pricing solutions that focus on securities that breach the fund mandate rather than adhere to it. Automated price collection and validation services, in particular, allow fund managers and administrators to carry out as many as 12 valuations over the course of a trading day. Before sending approved pricing data directly to the client’s fund accounting system they can also perform customized tolerance checks, such as on the percentage movement from a previous price or against a benchmark.

Operational objective #3: integrate systems

A high level of integration between transfer agency, accounting systems and pricing services can be highly advantageous for managing the operational implications of intraday valuation. Common tools and standards, integrated teams and a single source of data make it easier to coordinate activity and, in particular, carry out rigorous testing before new processes go live.

Operational objective #4: ensure global support

With cross-border trading constantly on the increase, global capabilities have never been so critical for money market fund operations. Reform, furthermore, is progressing at different speeds in different regions; in Europe, for example, a final decision on new rules is yet to be reached. As well as supporting cross-border distribution and regulatory variations, processing systems need to operate on a 24/7, real-time basis to manage the practical demands of trading across time zones.

Conclusion: get more from reform

While the largest organizations have already been galvanized into action, it is now up to the rest of the U.S. money market fund industry to tackle the major operational changes that reform will require. These include the increased integration of fund administration technology, from pricing and transfer agency components to fund accounting platforms, enabling firms to support multi-jurisdictional regulations with seamless efficiency.

In making such careful preparations, organizations of all sizes will be in a stronger position to not only manage reform but also benefit from it – as an opportunity to transform operations for the better.

For more on the operational challenges presented by U.S. money market fund reform, see the first article in our series, Putting money market fund reform into practice.
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