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A Negative Sign of the Times: Form N-MFP Can Report Negative Yields

On April 7, 2020, the Securities and Exchange Commission (the "SEC") [announced](#) an update to the EDGAR system that would allow negative values to be entered in Item C.17 of [Form N-MFP](#). Money market funds use Form N-MFP to report information to the SEC as of the end of each month. Item C.17 requires, for each security held by the fund, "[t]he yield of the security as of the reporting date." The change was prompted by the recent downturn in rates for one-month and three-months Treasury bills, which may also have prompted some Treasury money market funds to restrict new investments.

How Yields Become Negative

Treasury bills do not pay interest; their return comes from the difference between the price paid for the T-bill and the face amount paid at maturity. If you buy a \$100 face amount three-month T-bill for \$99.70, then you earn 30 cents when the T-bill matures. If you purchase this T-bill at issuance, this would translate to an annualized yield of a little more than 1.2%. What if you pay more than \$100 for this T-bill? For example, if you paid \$100.02, you would lose two cents when the T-bill matured. If you paid this much at issuance, it would translate to an annualized yield of -0.08%. One-month and three-month T-bills [traded above their face values](#) for part of the day on March 25, 2020, although they ended the day at or slightly above zero. So the prospect of negative yields is real.

Reporting Negative Yields

Readers will note that the yield on a T-bill depends on what you pay for it, not what it traded for at some other time. A money market fund that bought the three-month T-bill for \$99.70 will earn 30 cents when the bill matures, even if the bill subsequently trades for \$100.02. Nevertheless, for reasons I've never fathomed, Form N-MFP requires funds to report yields "as of" the date of the report. This appears to be the yield based on the current market value of the security. Footnote 1472 of the [release](#) that included Item C.17 in Form N-MFP explained that:

Because yield at purchase would be disclosed in a separate item, we proposed to delete the reference to "(including coupon or yield)" from current Form N-MFP Because ... we are not adopting the lot level reporting requirements we proposed, ... to facilitate use of the data collected and to clarify the time that the yield of the security must be calculated (as of the Form N-MFP reporting date), we are moving the question about yield out of the title question and adopting it as a standalone response."

This suggest that, if the market value of a security at the end of a month would produce a negative yield, this must be reported by the fund in response to Item C.17 even if the fund will earn a positive return from the security.

Negative Yields Can Be a Problem

From a credit perspective, the safest type of money market fund is a "Treasury-only" fund: a fund that invests solely in full, faith and credit obligations of the U.S. Treasury. Investors tend to regard these obligations as "risk free" in terms of payment at maturity. But these securities are not free of market risk: their prices go up and down throughout the day. If a fund invests exclusively in these securities, then its returns will depend on what it pays for them. As illustrated above, if the fund pays more than the face amount, it is sure to lose money when the

security matures. Such losses will erode the net asset value of a fund, which is not a good thing for a money market fund seeking to maintain a stable net asset value. The demand for Treasury securities that produces negative yields also causes investors to pour money into Treasury-only money market funds. This new money is useless if the fund cannot invest it at a positive return that at least covers the marginal increase in the fund's expenses. As the average weighted maturity ("WAM") of a money market fund cannot exceed 60 days, there is a limit to how much a Treasury-only fund can invest in longer-dated, higher yielding, securities. Thus, it may be best to curtail cash inflows into a Treasury-only fund when yields for Treasury securities maturing in 60 days or less are very low, and particularly when they are negative. This may explain why [Fidelity recently closed three money funds](#), two of which were Treasury-only, to new investors. Other funds may need to consider this option if rates dive again.

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