The Money Market Alternative

Money market funds became popular in the late 1970s when interest rates began to rise and investors received returns comparable to more traditional investment mechanisms. In recent years, their competitive historical rates of return, coupled with the growth of **mutual fund** families, have further increased the popularity of money market funds. These funds have become a flexible and liquid alternative to conventional savings methods such as checking accounts or bank certificates of deposit (CDs). While CDs are generally federally insured up to $100,000, mutual funds—including money market funds—fluctuate in value. Money market funds are neither insured nor guaranteed by the U.S. government.

Many individuals have checking accounts in which they maintain a high balance and only, on occasion, write a check. These larger accounts are sometimes used as a special account for property management or home emergencies. Money market funds offer the same liquidity as traditional checking accounts. However, in most instances, there is the potential for higher rates of return with these funds.

In addition, unlike a bank CD which penalizes you for early withdrawals, you may make contributions and redemptions at anytime with a money market fund. However, some funds may impose a minimum on the *size* of the transactions you make. In many cases, this minimum is $500, though some funds require a minimum of as little as $1. Money market funds also usually require a minimum balance for keeping the account open.

Money market funds can be an especially useful tool when making larger investments in a mutual fund family. By initially placing your investment into a mutual fund family's money market fund, your money can be dispersed—over several months for example—to any mutual fund within the same fund family. Therefore, while earning a modest return from your money market fund, you have the ability to execute the basic investment strategy of **dollar cost averaging**.

When you buy shares in a money market fund, the shares are, in turn, invested in a variety of short-term securities that earn market rates of interest. Money market funds vary according to the type of securities in which they invest. Generally, the funds keep a small portion of the earnings, usually 0.50% to 0.75%, as a management fee. The remainder of the earnings is passed on to you, the shareholder.

Since you are dealing with a fund, you need to know how it is valued. The **net asset value (NAV)** of each share normally remains at $1. There can be no assurance that a money market fund will be able to maintain a stable net asset value of $1.00 per share. For $1,000 you generally get 1,000 shares. Any earnings are also paid in shares. For example, suppose you invest $1,000 in a fund for one year and the fund earns 4%. At the end of the year, you own 1,040 shares worth $1,040. Thus, for all practical purposes, this structure is the same as if you had put money into a bank account earning 4%.

An investment in a money market fund is not insured or guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. Although such funds seek to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the fund. Remember that mutual funds are sold by prospectus, which includes important information on charges, expenses, and risks. To receive a current prospectus, contact your registered representative. Always read the prospectus carefully *before* investing.

Money market funds can be useful for a wide array of purposes. You may require a large liquid account, or may be interested in investing in several mutual funds within a specific mutual fund family. Or, perhaps, you would rather place your savings in a mechanism that offers the potential for more favorable returns without “locking up” your money for a fixed period of time. Even in varying situations, a money market fund can be an alternative to traditional savings methods.

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