

## PUBLIC STATEMENT

### **ESMA's guidelines on stress test scenarios under the MMFR continue to be applicable until their 2020 update**

1. Article 28(7) of the Money Market Funds Regulation (MMFR)<sup>1</sup> provides that the European Securities and Markets Authority (ESMA) shall develop guidelines with a view to establishing common reference parameters of the stress test scenarios to be included in the stress tests that Money Market Funds (MMFs) or managers of MMFs are required to conduct. These guidelines shall be updated at least every year taking into account the latest market developments. ESMA published the latest update of these guidelines on 19 July 2019<sup>2</sup> and their translations on 3 March 2020<sup>3</sup> ("2019 Guidelines").
2. The COVID-19 crisis has been challenging for MMFs. Risks have globally increased for MMFs and the money market instruments in which they invest. A number of EU MMFs faced significant liquidity issues during the period of acute stress in March 2020. This was particularly the case for some of the Low Volatility Net Asset Value (LVNAV) MMFs in USD and some Variable Net Asset Value (VNAV) MMFs in EUR, which faced heightened redemptions while on the asset side the liquidity of money markets deteriorated.
3. In this context, ESMA assessed whether the scenarios envisaged in the 2019 Guidelines are still appropriate in the current environment. The 2019 Guidelines include a specific liquidity shock on money market instruments, large redemptions and an increase in credit spread for government and corporate bonds, which are similar to the recent market stresses encountered during the Covid-19 crisis. Furthermore, when managers of MMFs conduct the stress test scenarios, they have to consider the current market rates and add up the shocks specified in the Guidelines. Therefore, applying the 2019 scenarios in the current market environment generally leads to absolute levels of stress similar to the levels observed in March. However, for some parameters, the 2019 scenarios have been

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<sup>1</sup> Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds (OJ L 169, 30.06.2017, p. 8).

<sup>2</sup> Final Report on Guidelines on stress test scenarios under the MMF Regulation ([ESMA34-49-164](#)).

<sup>3</sup> [ESMA34-49-172](#)

exceeded by the extreme market movements observed during the COVID-19 crisis and the relevant factors will be updated accordingly.<sup>4</sup> This is notably the case of the redemption scenario, as some funds exceeded the 25% redemption rate for professional investors specified in the guidelines.

4. ESMA is announcing today that the 2019 Guidelines will be updated in 2020 and the risk parameters<sup>5</sup> will be modified in light of the recent market developments. For that purpose, ESMA will work in collaboration with the ESRB and the ECB for the calibration of the risk parameters. ESMA expects to publish the 2020 update of the guidelines in Q4 2020. The guidelines will be further translated after the release of the update. Considering that the scenarios will reflect the assessment of systemic risk by ESMA, the ESRB and the ECB, ESMA is not planning to conduct a public consultation on the update of the guidelines.<sup>6</sup>
5. Against this background, ESMA confirms that the 2019 Guidelines and the scenarios calibrated therein will continue to apply until the 2020 updated version of the guidelines applies. The 2019 scenarios essentially capture the main risks MMFs have been facing during the acute phase of the crisis. In a second step, the 2020 update will focus on some specific parameters that need to be revised in light of the 2020 COVID-19 crisis.
6. Managers of MMFs are expected to include the results of the stress tests in the reports to be sent to National Competent Authorities (NCAs) through the reporting template. The Guidelines include stress test scenarios in relation to hypothetical changes in MMFs':
  - liquidity levels;
  - credit and interest rate risks;
  - redemptions levels;
  - widening/ narrowing of spreads among indexes to which interest rates of portfolio securities are tied; and
  - macro-economic shocks.

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<sup>4</sup> Notwithstanding what previously indicated in the revised [2020 ESMA Annual Work Programme](#), the severity of market conditions during the acute phase of the crisis, and the need to assess MMFs' preparedness to a similar stress episode, led ESMA and ESRB to decide to update some parts of the scenarios.

<sup>5</sup> Referred to in section 5 of the Guidelines on stress test scenarios under the MMF Regulation.

<sup>6</sup> The initial calibration of the stress scenarios was not part of the previous consultation.

7. In the interim, pending the 2020 update, all the sections of the 2019 Guidelines will continue to apply, including the internal stress test exercise to be carried out by managers of MMFs. Article 28(1) of the MMFR provides that “*Each MMF shall have in place sound stress testing processes that identify possible events or future changes in economic conditions which could have unfavourable effects on the MMF*”. These internal stress tests could include other factors than those referred to in the 2019 Guidelines, and when designing these internal stress tests, ESMA expects that MMFs would factor in the impact of the recent market stress according to the risk profile of their fund.
  
8. ESMA, together with the NCAs, will continue monitoring developments in the MMF sector.