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S&P Downgrade Not Expected to Have Significant Impact on Money Funds

Citing inadequate progress in slowing the growth of America's debt, Standard & Poor's reduced the U.S. government's long-term sovereign debt rating from AAA to AA+ on Friday, August 5, 2011. BofA Global Capital Management believes that while potentially significant for the fixed income markets and the U.S. economy over the long-term, the downgrade is unlikely to have a significant impact on money market funds given that S&P affirmed its top rating for U.S. short-term debt.

In explaining its rationale for the downgrade, S&P said last week's $2.4 trillion debt ceiling agreement was not sufficient to stabilize the country's medium-term "debt dynamics." It also expressed skepticism about the ability of policy makers to achieve the $4 trillion of debt reduction that S&P had said was necessary to avoid a downgrade.

Typically, a debt downgrade pressures the prices of the affected securities, but the S&P downgrade may have a relatively minor impact on Treasury prices because investors likely will continue to view U.S. issues as low-risk, highly liquid securities that are likely to offer stability during market disruptions. As such, we at BofA Global Capital Management do not foresee a significant impact on the valuation of government securities or the functionality of the market for repurchase agreements. That said, we acknowledge the situation is fluid, which makes it difficult to fully evaluate the impact of S&P downgrade at this time.

Another important development stemming from the S&P downgrade of U.S. Treasuries is that securities issued by Fannie Mae, Freddie Mac and other government-sponsored entities (GSEs) were downgraded as well. The debt ratings of the GSEs historically have mirrored the credit rating for the U.S.'s long-term sovereign debt. In addition, select long-term municipal securities, such as pre-refunded bonds or housing bonds with mortgages guaranteed by the U.S. government or the GSEs may suffer a downgrade from S&P. The agencies' short-term debt rating did not change and remains A-1+.

Because S&P affirmed its A-1+ rating – the highest possible – for short-term U.S. debt and removed its rating on short-term U.S. issues rating from Credit Watch-negative status, we believe S&P's downgrade of the U.S.'s long-term debt rating will have only minimal impact on money funds, which can invest only in short-term credits. The stress tests we have conducted on our funds' portfolios revealed no adverse impact from a one- notch downgrade of U.S. long-term debt on the credit quality of our holdings or their eligibility for inclusion in money market funds. Finally, we believe that S&P is unlikely to downgrade the rating of money market funds with an AAA rating.

BofA Global Capital Management will continue to provide you with information on market developments that impact your investments with us. If you have any questions, please contact your client service officer or sales representative.

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