Money Market Account

What is a Money Market Account?

A money market account, or Money Market, or MMA, is a savings account that allows a limited number of checks to be drawn from the account each month. How much interest a money market account pays, and whether it's the highest-paying deposit product offered, varies for each account from bank to bank.

The money market is where financial instruments with high liquidity and very short maturities are traded. It is used by participants as a means for borrowing and lending in the short term, with maturities that usually range from overnight to just under a year. Among the most common money market instruments are eurodollar deposits, negotiable certificates of deposit (CDs), bankers acceptances, U.S. Treasury bills, commercial paper, municipal notes, federal funds and repurchase agreements (repos).

A money market account is a type of savings account, with the same protections and generally a slightly higher interest rate. The trade-off? There's usually a higher minimum balance requirement.

Money market transactions are wholesale, meaning that they are for large denominations and take place between financial institutions and companies rather than individuals. Money market funds offer individuals the opportunity to invest smaller amounts in these assets.

The money market is a subsection of the fixed income market. We generally think of the term fixed income as being synonymous to bonds. In reality, a bond is just one type of fixed income security. The difference between the money market and the bond market is that the money market specializes in very short-term debt securities (debt that matures in less than one year).

Money market investments are also called cash investments because of their short maturities.

Money market securities are essentially IOUs issued by governments, financial institutions and large corporations. These instruments are very liquid and considered extraordinarily safe. Because they are extremely conservative, money market securities offer significantly lower returns than most other securities.

One of the main differences between the money market and the stock market is that most money market securities trade in very high denominations. This limits access for the individual investor.

The money market is a dealer market, which means that firms buy and sell securities in their own accounts, at their own risk. Compare this to the stock market where a broker receives commission to acts as an agent, while the investor takes the risk of holding the stock. Another characteristic of a dealer market is the lack of a central trading floor or exchange. Deals are transacted over the phone or through electronic systems.

The easiest way for us to gain access to the money market is with a money market mutual funds, or sometimes through a money market bank account. These accounts and funds pool together the assets of thousands of investors in order to buy the money market securities on their behalf. However, some money market instruments, like Treasury bills, may be purchased directly. Failing that, they can be acquired through other large financial institutions with direct access to these markets.

Where Money Market Accounts Came From

A few decades ago, there was a legal cap set by the government on the interest rates a bank could offer customers. Banks couldn't try to outdo one another by offering higher rates, so instead they sold themselves with good customer service and free swag like toasters and slow cookers for new account holders.

Capped rates became unworkable in the early 1980s. Market interest rates were rising, but savings rate caps stayed relatively low in order to help banks, which had made many loans at lower interest rates in previous years, stay afloat by limiting how much they had to pay out in interest to customers.

In response, consumers seeking higher rates took their money out of the banks and put it into money market mutual funds that paid market rates of interest. These funds invested in short-term debt securities but were not federally insured like bank accounts.

Still, consumers' savings flowed out of banks, leaving them with little money to lend out and eventually forcing Congress to pass the Garn-St. Germain Depository Institutions Act of 1982. That law let banks offer money market deposit accounts that paid a "money market" rate of interest to attract deposits, rather than a capped savings rate.

What Money Market Accounts Do

At their core, MMAs are basically just a type of savings account, with some minor variations. How much interest an MMA pays, and whether it's the highest-paying deposit product offered, varies from bank to bank.

The best way to think of MMAs is as a hybrid of checking accounts and savings accounts, It comes under the umbrella of savings, but it has limited checking capabilities, which makes it more attractive than just pure savings accounts

A money market account is a savings account that allows you to make up to 6 transactions a month out of it, It's different from a checking account because a checking account is unlimited."

And don't worry about losing your balance if the bank fails. Like savings and checking accounts, money market accounts are federally insured.

Comparing account features			
	Savings	Checking	Money market account
FDIC-insured	✓	✓	✓
You get a checkbook for withdrawal		✓	✓
You get a debit card for withdrawal	✓	✓	✓
Limited transactions	✓		✓
Unlimited transactions		✓	

Money Market Accounts Are Still in Demand

The transactional capabilities of MMAs look pretty pathetic compared with a typical rewards checking account, which can pay substantially more in interest each month with no limitations on the number of transactions you can make.

Some banks are beginning to pay more interest on savings account deposits than MMAs, making money market accounts seem ever more redundant.

But in recent years, MMAs have held record amounts of Americans' cash, in the trillions of dollars due to the uncertainty about the economy among consumers

Money Market Participants

Institutions that participate in the money market include banks that lend to one another and to large companies in the eurocurrency and time deposit markets; companies that raise money by selling commercial paper into the market, which can be bought by other companies or funds; and investors who purchase bank CDs as a safe place to park money in the short term.

The U.S. government issues Treasury bills in the money market, and the bills have maturities that range from a few days to one year. Only primary dealers can buy them directly from the government; dealers trade them between themselves and sell retail amounts to individual investors. State, county and municipal governments also issue short term notes.

Commercial paper is a popular borrowing mechanism because it is exempt from SEC registration requirements. It's attractive to corporate investors because rates are higher than for bank time deposits or Treasury bills, and a range of maturities is available, from overnight to 270 days. However, the risk of default is significantly higher for commercial paper than for bank or government instruments.

Money Market Funds

A money market fund's purpose is to provide investors with a safe place to invest easily accessible, cash-equivalent assets.

It is a type of mutual fund characterized as a low-risk, low-return investment.

Since money market funds have relatively low returns, investors such as those participating in employer-sponsored retirement plans, might not want to use money market funds as a long-term investment option because they will not see the capital appreciation they require to meet their financial goals.

Money Market Pros and Cons

Aside from being low risk and highly liquid, money market funds may be attractive to investors because they have no loads, which are fees mutual funds may charge for entering or exiting the fund.

Some money market funds also provide investors with tax-advantaged gains by investing in municipal securities that are tax-exempt at the federal and/or state level.

A money market fund might also hold short-term U.S. Treasury securities, such as T-bills; certificates of deposit (CDs); and corporate commercial paper.

A downside of money market funds is they are not covered by federal deposit insurance. Other investments with comparable returns, such as money market deposit accounts, online savings accounts and certificates of deposit, are covered. However, money market funds are considered safe investments and are regulated under the Investment Company Act of 1940.

Money Market Quick Facts

The money market specializes in debt securities that mature in less than one year.

Money market securities are very liquid, and are considered very safe. As a result, they offer a lower return than other securities.

The easiest way for individuals to gain access to the money market is through a money market mutual fund.

A certificate of deposit (CD) is a time deposit with a bank. CDs are safe, but the returns aren't great, and your money is tied up for the length of the CD. CDs are generally issued by commercial banks but they can be bought through brokerages. They bear a specific maturity date (from three months to five years), a specified interest rate, and can be issued in any denomination, much like bonds. Like all time deposits, the funds may not be withdrawn on demand like those in a checking account. CDs offer a slightly higher yield than T-Bills because of the slightly higher default risk for a bank but, overall, the likelihood that a large bank will go broke is pretty slim. Of course, the amount of interest you earn depends on a number of other factors such as the current interest rate environment, how much money you invest, the length of time and the particular bank you choose. While nearly every bank offers CDs, the rates are rarely competitive, so it's important to shop around.

Money Market – When Should You Consider One?

Don’t expect to see quick gains on any of the four primary types of bank accounts: checking, savings, money market and CDs. Other investment options are better suited to that end, although not everyone feels comfortable with the volatility of the stock market.

The situation where a money market account is your best option is fairly specific. It’s a good choice if you want:

- The safety of a bank or credit union.
- A higher interest rate.
- Access to funds in a pinch.
- The ability to write a few checks.

If any of those aren’t true (and sometimes even then), you can find better alternatives elsewhere.

For example, if you want growth but greater access to your money, you may be better off opening an interest-bearing checking account. If you don’t care about writing checks, you can find comparable or better rates with some high-yield online savings accounts. And if you just want the bank account with the highest return and can afford to set this money aside for months or years, try a CD.

You could use a money market account for an emergency fund. Like a basic savings account, it’s separate from your daily use, but the money market account might grow a bit faster and you can write a check from it to cover whatever surprise arises.

What to Look for in a Money Market Account

The best money market accounts come with high yields, low minimum balances, few fees and the right amount of access to your funds. Shop around to find the best rates and evaluate what different banks and credit unions, in your area and online, are offering.

A money market account can be a good place to park your cash. There are some limitations, but it’s a option worth considering if you want to see your money grow in a safe environment.

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