

Mini-case 5: Participants in the Money Markets, Weighted Average Returns, Foreign Alternatives

CONCEPTS IN THIS CASE

money market securities
treasury bills
overnight funds
repurchase agreements
negotiable CDs
commercial paper
Eurodollars
London interbank bid and offer rate
money market mutual funds

You have just been named as a beneficiary in a will. The initial amount is \$2 million dollars. Due to poor estate planning, the executor must pay federal, provincial and local income taxes, estate (death) taxes, probate costs, and other fees. This costs you \$900 000. You are not ready to commit your funds for the long run, since you do not know where you will be or what you will be doing in the future. You want to invest the funds in the money market as a “warehouse” until you are ready to make long-term decisions on your future. With this in mind, you begin to study the market for short-term securities that mature in one year or less from their original issue date. Your goal is to maximize your return for one year while minimizing risk and maintaining trading flexibility.

1. To achieve your goal, you begin by answering the following questions:

- a. Who are the major players in the money market?
- b. What are the primary money market instruments?

2. All investments are based on one-year maturities or actual returns, beginning on the first day of business for the calendar year and ending on the last day of business for the same calendar year. You obtain the rates and share prices for the first and last business days for the previous calendar year, using library resources, the Internet, or other databases. (If you use the Internet, for commercial paper, CDs, and treasury bills, check out these websites: www.bankofcanada.ca, www.tdcanadatrust.com/invest/moneymkt, www.canada.etrade.com, www.treasurybills.ca, www.hsbc.ca, www.bmo.ca/economic/monetary.html, and www.rbcd.com/mm.html)

- a. What is the weighted average expected rate of return for all investments made in January?
- b. What is the weighted average actual rate of return for all investments ending in December?
- c. What is the weighted average expected rate of return for all investments between January and July 1?
- d. What is the weighted average actual rate of return for all investments between January and July 1?
- e. Which holding period would you prefer, 6 months or 12 months?

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