The Danger of Money Market Accounts

After a decade of money market rates hovering around zero, the sudden ability to earn 5% on cash with no investment risk and no default risk while maintaining full liquidity seems like an incredible opportunity especially compared to a couple of years ago.

The problem is that many long-term investors are treating the money market as the temporary solution to their long-term investment goals. Currently, there is about $6 trillion parked in money market which is at historical, all-time highs.  The fact of the matter is that the Federal Reserve has announced that their plan is to cut interest rates as soon as it feels it is appropriate.

The bond markets are pricing in an 83% chance that the first-rate cuts will start in May and that rates will be cut to 3.9% by the end of the year, and even lower the following year. That means that the money market rates could be down to 3.5% by January.

Given this widely available information, how many money market investors would like to lock in their 5% money market rates for the next 5, 10, or even 15 years?

Unfortunately, you can’t lock in your money market rates, but you can lock in over 6% from insurance companies while rates are high.  You can also lock in over 7.5% on private preferred stock for the next five years and you can earn over 10% on private credit funds.

Many money market investors are lulled by a false sense of security of the temporary high money market rates.  They are thinking, “Why should they do anything else?”  The reality is when rates drop to 3% money market investors will start looking for alternatives.  However, at that time the drop-in interest rates will also have lowered the rates on the alternatives that I just alluded to.

Therefore, for money that they don't need to spend or live on in the next few years, I am recommending to our clients to reallocate their money market into higher yielding alternatives **before** the Federal Reserve lowers interest rates as they indicated they will be doing as soon as it is practical.

\*Barrons

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