

# Money Markets Overview & Outlook

September 30, 2011



**J. Brian Henderson, CFA**  
*President*

Mr. Henderson established Cavanal Hill Investment Management's (Cavanal Hill) fixed income philosophy and process in 1993 while serving as the firm's Director of Fixed Income Strategy and as a Portfolio Manager for the taxable and tax-exempt fixed income and money market strategies. Prior to joining Cavanal Hill, Mr. Henderson was the Head Taxable Fixed Income Trader for Bank of Oklahoma's Capital Markets group. Mr. Henderson received a Bachelor of Business Administration in Finance from Southern Methodist University in 1989.

## Keys to Watch

- Economic data
- Federal Reserve action
- European Union policy

### Q: How did the yield environment change during the quarter?

**A:** Investors continued to face a challenging yield environment during the third quarter, as macroeconomic factors deteriorated and yields remained historically low. In particular, economic growth slowed, triggering renewed recession fears, while Europe's mounting sovereign debt problems and fears of a default in Greece put the entire financial sector under pressure. Meanwhile, in late-July, the U.S. government approached its debt ceiling, prompting a contentious debate over raising the nation's borrowing limit. The deliberations raged on, and Treasury bill yields inched upward on worries about a Congressional stalemate and potential U.S. government default. Congress eventually reached an agreement to raise the debt ceiling, and within days, Standard & Poor's

**In this environment, the Fed committed to keeping the federal funds rate target at its historically low range (0% to 0.25%) through mid-2013**

downgraded the nation's long-term credit rating, sending shockwaves through the financial markets and triggering a flight to quality that—despite the downgrade—sent U.S. Treasury yields tumbling.

In this environment, the Federal Reserve (the "Fed") committed to keeping the federal funds rate target at its historically low range (0% to 0.25%) through mid-2013. In addition, the Fed launched another stimulus program, "Operation Twist," designed to lower long-term interest rates while keeping short-term rates at current or higher levels.

Despite spiking during the debt ceiling debate, the three-month Treasury bill yield declined for the entire quarter, starting the period at 0.03% and falling to 0.02% on September 30, according to the U.S. Treasury web site. On the other hand, money market yields tied to the three-month LIBOR<sup>1</sup> increased during the quarter, due to the sovereign

debt concerns in Greece and other peripheral European nations. The three-month LIBOR started the three-month period at 0.25% and ended it at 0.37%, according to Bloomberg.

### Q: How did the municipal money market fare?

**A:** Early in the quarter, seasonal issuance by state and local governments boosted the supply of fixed-rate notes in the one-year maturity range. But, overall, municipal money market yields remained historically low during the quarter. For example, the SIFMA Index<sup>2</sup>, a weekly benchmark of the average yields on variable-rate demand notes (VRDNs), fell to an all-time low of 0.07% in July. Rates moved slightly higher during the quarter, but investors generally struggled to find yield in the money market portion of the municipal market. In addition, due to the uncertainty plaguing the European banking system, many money market funds trimmed their exposure to European bank letter of credit providers on VRDNs.

(Continued on page 2)

<sup>1</sup> The London Interbank Offered Rate (LIBOR) is the average rate charged by large banks in London for loans to each other. LIBOR is a relatively volatile rate and is typically quoted in maturities of one month, three months, six months and one year.

<sup>2</sup> Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Index, produced by Municipal Market Data (MMD), is a 7-day high-grade market index comprised of tax-exempt variable rate demand obligations (VRDO's) from MMD's extensive database. SIFMA is a leading securities industry trade group representing securities firms, banks, and asset management companies in the U.S. and Hong Kong.

**An investor should consider a fund's investment objectives, risk and charges and expenses carefully before investing or sending money. This and other important information about an investment company can be found in the fund's prospectus. To obtain a Cavanal Hill Funds prospectus or summary prospectus, please call 800-762-7085. Please read it carefully before investing.**

The Funds are distributed by BOSC, Inc., an SEC registered investment adviser, a registered broker/dealer, member FINRA/SIPC. SEC registration does not imply a certain level of skill or training.

Cavanal Hill Investment Management, Inc. is an SEC registered investment adviser and a wholly-owned subsidiary of BOKF, NA, a wholly-owned subsidiary of BOK Financial Corporation, a financial holding company ("BOKF"). SEC registration does not imply a certain level of skill or training. BOKF, NA serves as the custodian for the Cavanal Hill Funds. BOKF holdings also include BOSC, Inc., the distributor for the Cavanal Hill Funds. Cavanal Hill Investment Management, Inc. provides investment advice, administration and other services for the Funds and receives a fee for providing such services as fully described in the prospectus. Bank of Oklahoma and its affiliates Bank of Arkansas, Bank of Albuquerque, Bank of Texas, Southwest Trust Company, Bank of Arizona, Bank of Kansas City and Colorado State Bank and Trust offer investment management and administrative services nationally and administer more than \$30 billion in assets for numerous clients, including foundations and endowments, and high-net-worth individuals. The Funds are distributed by BOSC, Inc., an SEC registered investment adviser, a registered broker/dealer, member FINRA/SIPC. SEC registration does not imply a certain level of skill or training.

MUTUAL FUNDS AND OTHER INVESTMENTS: NOT FDIC INSURED • MAY LOSE VALUE • NO BANK GUARANTEE 10/11



**Q: What is your outlook for the taxable and tax free money markets?**

**A:** We expect money market rates to remain extremely low for the intermediate term, as the Fed has committed to holding rates steady in the face of a slowing economy, high unemployment and a weak housing market. In addition, uncertainty in Europe will likely contribute to a cautious sentiment among investors.

***Money market funds seek to preserve the value of your investment at \$1 per share, however, it is possible to lose money by investing in a money market fund. An investment in a money market fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any government agency.***

*The Fund's income may be subject to certain state and local taxes and, depending on one's tax status, to the federal alternative minimum tax.*

---

**An investor should consider a fund's investment objectives, risk and charges and expenses carefully before investing or sending money. This and other important information about an investment company can be found in the fund's prospectus. To obtain a Cavanal Hill Funds prospectus or summary prospectus, please call 800-762-7085. Please read it carefully before investing.**

An investment in the Cavanal Hill Funds is not a deposit or an obligation of Bank of Oklahoma, its affiliates, or any bank and it is not insured or guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other governmental agency. Investors should carefully consider the investment objectives, risks, charges, and expenses of a fund before investing. For a prospectus containing this and other important information for any Cavanal Hill Fund product, call your financial representative, call the Cavanal Hill Funds at 1-800-762-7085 or go to [www.cavanalhillfunds.com](http://www.cavanalhillfunds.com). The Cavanal Hill Funds are distributed by BOSC, Inc., member of FINRA and SIPC, and a subsidiary of BOK Financial Corp. Fund portfolio holdings are subject to change and do not represent any type of recommendation.

Cavanal Hill Investment Management, Inc. is an SEC registered investment adviser and a wholly-owned subsidiary of BOKF, NA, a wholly-owned subsidiary of BOK Financial Corporation, a financial holding company ("BOKF"). SEC registration does not imply a certain level of skill or training. BOKF, NA serves as the custodian for the Cavanal Hill Funds. BOKF holdings also include BOSC, Inc., the distributor for the Cavanal Hill Funds. Cavanal Hill Investment Management, Inc. provides investment advice, administration and other services for the Funds and receives a fee for providing such services as fully described in the prospectus. Bank of Oklahoma and its affiliates Bank of Arkansas, Bank of Albuquerque, Bank of Texas, Southwest Trust Company, Bank of Arizona, Bank of Kansas City and Colorado State Bank and Trust offer investment management and administrative services nationally and administer more than \$30 billion in assets for numerous clients, including foundations and endowments, and high-net-worth individuals. The Funds are distributed by BOSC, Inc., an SEC registered investment adviser, a registered broker/dealer, member FINRA/SIPC. SEC registration does not imply a certain level of skill or training.

Information contained herein has been obtained from sources believed to be reliable, but not guaranteed. The opinions expressed herein reflect the judgment of the authors at this date and are subject to change without notice and are not a complete analysis of any sector, industry or security. This document contains forward-looking statements that are based on management's beliefs, assumptions, current expectations, estimates, and projections, the securities and credit markets and the economy in general. Words such as "anticipates," "believes," "estimates," "expects," "forecasts," "plans," "projects," variations of such words and similar expressions are intended to identify such forward-looking statements. Management judgments relating to and discussion of the value and potential future value or performance of any security, group of securities, type of security or market segment involve judgments as to expected events and are inherently forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict with regard to timing, extent, likelihood and degree of occurrence. Therefore, actual results and outcomes may materially differ from what is expressed, implied, or forecasted in such forward-looking statements. The potential realization of these forward-looking statements is subject to a number of limitations and risks. Cavanal Hill does not undertake any obligation to update, amend, or clarify forward-looking statements, whether as a result of new information, future events or otherwise.

Commentary provided is for the period ended 9/30/2011, is designed to provide a frame of reference and does not constitute investment advice. Information contained herein has been obtained from sources believed to be reliable, but not guaranteed. The opinions expressed herein reflect the judgment of the authors at this date and are subject to change without notice and are not a complete analysis of any sector, industry or security.

**MUTUAL FUNDS AND OTHER INVESTMENTS: NOT FDIC INSURED • MAY LOSE VALUE • NO BANK GUARANTEE**

10/11