WELLS FARGO Asset Management

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PORTFOLIO MANAGER COMMENTARY

Overview, strategy, and outlook

As of June 30, 2020

Money market overview

If the end of the first quarter of 2020 felt like deja vu all over again, the second quarter positively felt like a renaissance. As we watched the tremendous risk-off trades and liquidity raising taking place in March, we couldn't help but flash back to 2016 and the implementation of money market reform, which saw institutional prime funds shrink by over 86%, bottoming out that year at just north of $119 billion. While that was clearly a regulatory-driven event, the pandemic-related selling we saw in the prime funds was prompted by a confluence of a few different factors: investors raising cash to meet liquidity needs, shareholders conducting precautionary cash raises in case fees and/or gates were implemented, falling net asset values (NAVs) in institutional floating NAV (FNAV) funds due to market dislocations, and a general flight to perceived safety in the face of the uncertain effects of the coronavirus on the economy. Some funds were hit harder than others—institutional versus retail—as were different fund families. But by and large, with only one exception, funds were able to manage their liquidity in excess of the 30% regulatory requirement, and all funds avoided implementing fees and gates. The Federal Reserve (Fed) played a vital role in ensuring this outcome and helping calm the financial markets with the implementation of its Money Market Mutual Fund Liquidity Facility (MMLF), which went operational on March 23, and outflows from prime funds ceased by the end of March. At the end of the day, so to speak, prime funds ended down over 15% on the month, with institutional prime funds down almost 19%.

And then a funny thing happened: Prime funds started growing again. Perhaps it was the yield advantage over government and Treasury funds as the Fed implemented its zero interest rate policy, driving those yields toward zero, or maybe the dislocated NAVs provided a potentially attractive total return play, or the possibility of fees and gates being instituted seemed more remote with the MMLF in place. In any event, investors began buying back prime funds: April inflows were $82 billion followed by another $87 billion in May, which then slowed to $23 billion in June. All in all, prime fund assets under management reached a post-reform high of over $1.1 trillion.

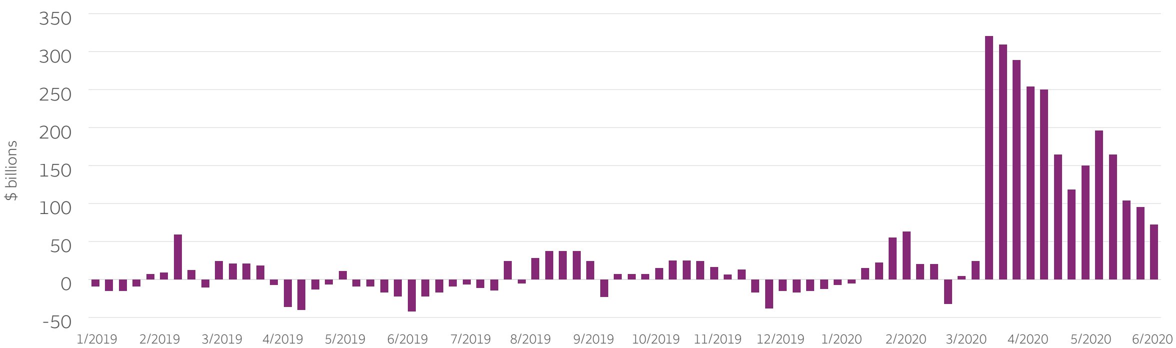
This focus on prime funds is not to downplay the tremendous growth of government funds during the past two quarters, which propelled the industry to record assets under management of over $5 trillion. It is meant to illustrate that in spite of market dislocations, there is still a demand on the part of some investors for this type of product. The course of asset flows as the year progresses, liquidity facilities wind down, and the inevitable talk of reform gets started will help us better understand the risk characteristics driving client flows and preferences and, in turn, help us better manage the funds to meet investor expectations.

Sector views

U.S. government sector

The government money markets were quiet in June, with volatility largely absent and the path of Treasury bill (T-bill) supply set to be the main driver of market yields. The Treasury has issued nearly $2.5 trillion in additional T-bills since it began funding its pandemic-related outflows in late March, but it has curiously raised a lot more money than it has spent. As shown in the chart below, although net supply has generally shrunk each week since the surge started, even these smaller weekly additions exceed previous issuance levels.

Weekly net new T-bill issuance



Source: U.S. Treasury

Because the Treasury hasn't yet spent as much as expected (a phrase not often written), its cash balance has risen to towering heights, reaching $1.6 trillion in late June from its usual level around $400 billion in March, as shown below.

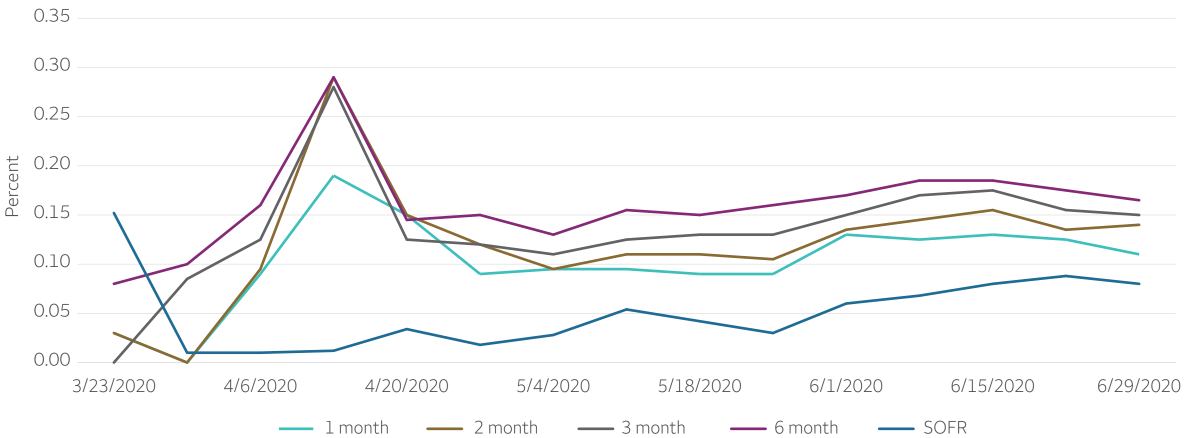
U.S. Treasury cash balance

Source: Bloomberg L.P.

The bloated cash balance will likely be addressed in the second half of the year, one way (increased spending) or another (reduced borrowing). The former may be the result of additional outlays under current legislation or new outlays on another rumored but not yet negotiated round of stimulus. As for borrowing, net decreases in T-bill supply may be just around the corner in July. There will be a couple of complicating factors. First, unless it is extended again, the due date for tax filings and payments of July 15 (already pushed back once from April 15) tends to result in large cash receipts by the Treasury. Second, although the Treasury initially used the T-bill market in its traditional stabilizer role as a quick way to raise cash, it will now proceed to term out the new debt, eventually reducing the T-bill share of its total debt.

Considering the Treasury's large cash balance, its tax season cash receipts, and the desire to term out the debt, it will not be surprising if the bulk of the year's net T-bill issuance is behind us. However, the continued positive supply did weigh on the market in June. As shown below, yields on both T-bills and repo edged up, but they did so in an exceedingly orderly fashion, with the volatility often seen in the past, especially in the repo market, largely absent.

Secured overnight financing rate (SOFR) and T-bill auction yields



Sources: Bloomberg L.P. and Wells Fargo Asset Management

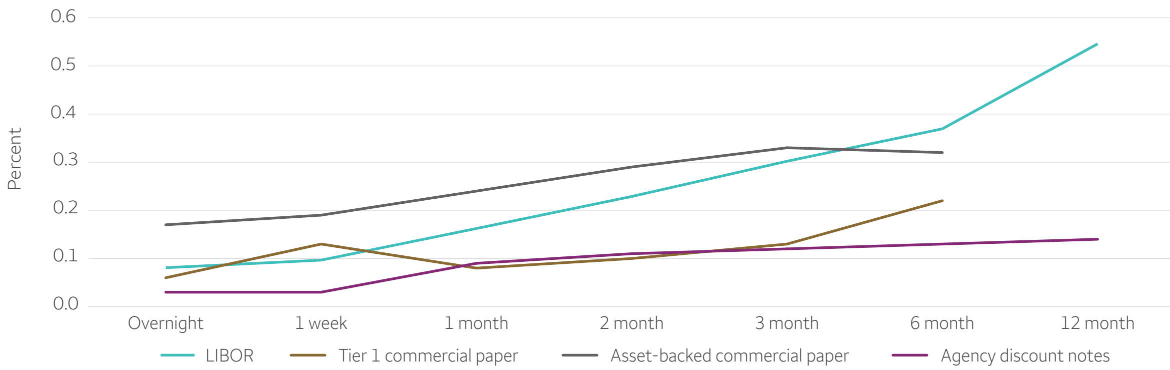
Prime sector

As expected, the Federal Open Market Committee (FOMC) left its target rate range unchanged at 0.00% to 0.25% at the conclusion of its June meeting. Market chatter prior to the meeting was that the FOMC might introduce further quantitative easing in the form of yield-curve control. In the end, however, the FOMC made no changes to its forward guidance, stating it expects "to maintain this target range until it is confident that the economy has weathered recent events and is on track to achieve its maximum employment and price stability goals." The rest of the policy statement characterized the current economic situation as mostly unchanged from the April FOMC meeting while acknowledging the "tremendous human and economic hardship" caused by the coronavirus. The statement also reiterated "sharp" declines in economic activity, a "surge" in job losses, and that weaker demand and lower oil prices are "holding down" inflation. And while it did mention the improvement in financial conditions and credit access relative to the prior meeting, it repeated that the health crisis will weigh "heavily" on economic activity, employment, and inflation in the near term and pose considerable risk to the medium-term economic outlook. In other words, policy will be on hold for a considerable period.

The FOMC also released its Summary of Economic Projections (SEP) for the first time since December 2019. As expected from the policy statement, the median projected path for the target rate showed no change from now through 2022. The median estimate of the longer-run target rate remained unchanged at 2.5%. The median gross domestic product (GDP) projection was -6.5% for 2020, +5.0% for 2021, and +3.5% for 2022. The longer-run GDP projection was 1.8%, down 0.1% from the December reading. Projections for unemployment in 2020 ranged from 7% to 14% with the median at 9.3%, 6.5% in 2021, and 5.5% in 2022. On the inflation front, the median expectation declined to 0.8% in 2020 (a decrease of 1.1% from the December expectation), 1.6% in 2021, and 1.7% in 2022. The SEP reinforces the members' beliefs that it will take some time for the economy to regain its footing from the economic shock delivered by the health crisis and that members are willing to be patient with policy to ensure the Fed's dual mandate is achieved.

In the money markets, assets continued to flow into money market complexes. As reported by Crane Data, prime assets grew almost another $23 billion this month on top of $88 billion last month, further increasing demand for money market securities. However, total not-seasonally-adjusted commercial paper outstanding dropped by roughly $39 billion this month on top of a roughly $40 billion drop last month as issuers opportunistically termed out liabilities to capture low rates in long-term markets. These supply/demand imbalances have created a favorable technical situation that is supportive of liquidity and asset performance in prime money markets as more dollars are chasing less product.

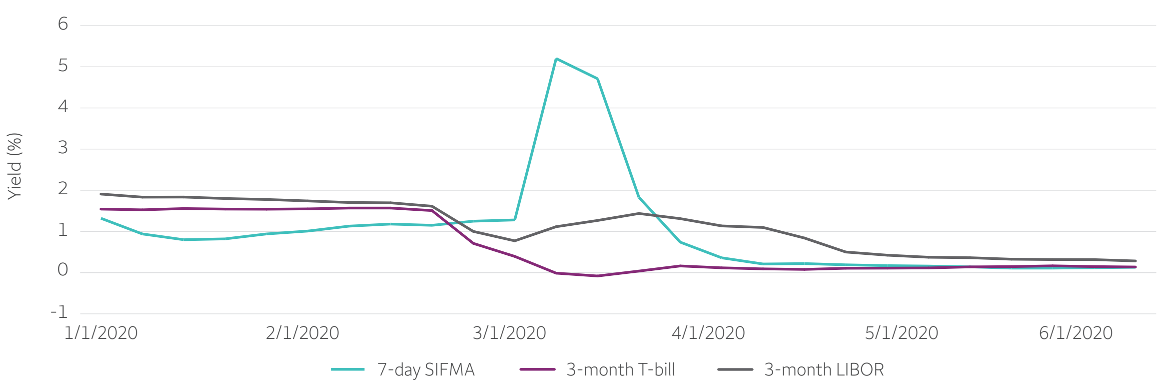
Money market yield curves, as of 6/30/2020



Sources: Bloomberg L.P. and Wells Fargo Asset Management

With the FOMC on hold and technical imbalances continuing, yields in money market securities continue to compress. The chart below demonstrates the impact of the coronavirus-driven market volatility that occurred in March and the quick recovery as investors reentered the various asset classes. Using the 3-month T-bill as a proxy for government funds, we saw yields plummet into negative territory as a result of risk-off sentiment only to see yields recover as liquidity returned to the markets and with the supply in the government space increased dramatically. On the other hand, municipal and prime funds saw yields spike in March only to recover and move lower as assets returned and liquidity improved. This yield compression is expected to grind tighter as the FOMC remains on hold in order to allow the economy to recover from the health crisis.

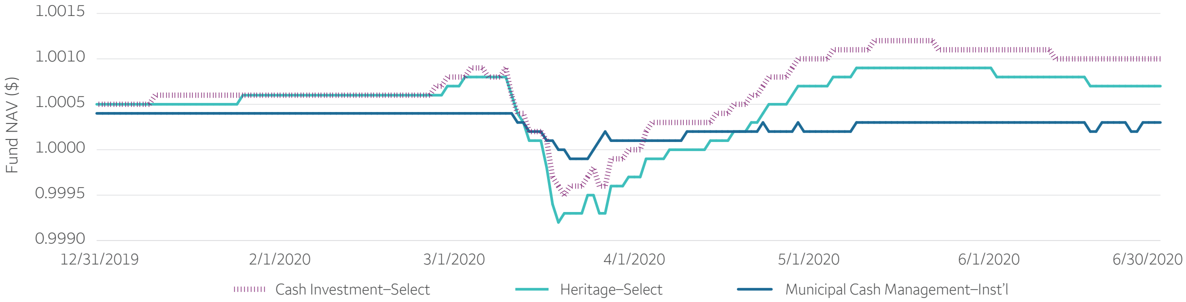
Money market yields, as of 6/24/2020



Sources: Bloomberg L.P. and Wells Fargo Asset Management

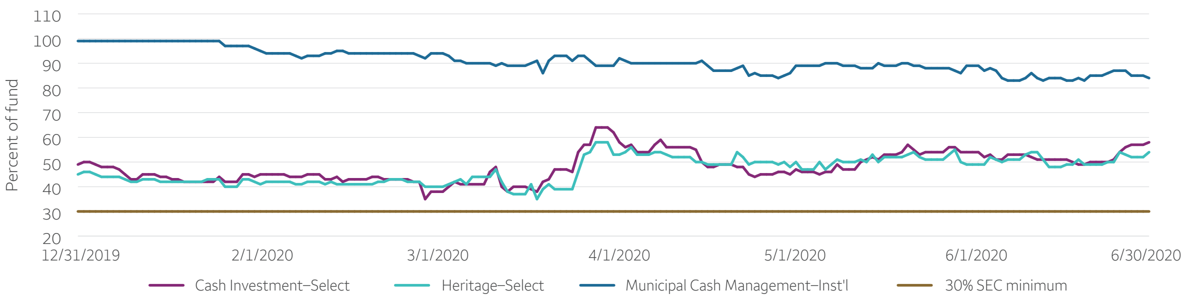
In the current environment, we favor our investment strategy of emphasizing higher levels of liquidity in our portfolios and extending where appropriate to capture higher yields. This additional liquidity buffer enhances our ability to meet the liquidity needs of our investors and helps stabilize NAV volatility while still allowing us to opportunistically add securities to lock in higher yields.

Wells Fargo FNAV money market fund NAVs



Source: Wells Fargo Funds

Wells Fargo FNAV money market fund weekly liquid assets



Source: Wells Fargo Funds

Municipal sector

Rates in the municipal money market sector continued to settle into a new lower-for-longer interest rate environment during June. Demand for variable-rate demand notes (VRDNs)[1] and tender option bonds (TOBs)[2] in the overnight and weekly space pushed the Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Index[3] down to a multiyear low of 0.11% on June 3, down from 0.14% at the end of May. Assets in municipal money market funds continued to trend lower with roughly $3.6 billion in outflows during the month, according to Crane Data. Any decrease in purchasing power from municipal money market funds was offset by demand from crossover buyers and municipal bond funds, which have seen a resurgence in inflows.

During the month, we continued to focus our purchases primarily in VRDNs and TOBs with daily and weekly puts. However, we have continued to opportunistically add exposure to fixed-rate securities as the onset of note season has led to an increase in supply on the long end. It is expected that cash flow borrowing needs for municipalities will be larger than usual due to coronavirus-related disruptions. Accordingly, the municipal yield curve remains somewhat steep as high-grade one-year notes closed out the month at 0.30%, unchanged from May.

On the horizon

We will be on hiatus for July, and commentary will resume after Labor Day. Enjoy your summer!

Rates for sample investment instruments—current month-end % (June 2020)

Sector	1 day	1 week	1 month	2 month	3 month	6 month	12 month
U.S. Treasury repos	0.07	0.08	–	–	–	–	–
Fed reverse repo rate	0.00	–	–	–	–	–	–
U.S. Treasury bills	–	–	0.12	0.12	0.13	0.15	0.15
Agency discount notes	0.03	0.03	0.09	0.11	0.12	0.13	0.14
LIBOR	0.08	0.10	0.16	0.23	0.30	0.37	0.55
Asset-backed commercial paper	0.17	0.19	0.24	0.29	0.33	0.32	–
Dealer commercial paper	0.06	0.13	0.08	0.10	0.13	0.22	–
Municipals	0.15	0.13	0.21	0.22	0.23	0.26	0.30

Sources: Bloomberg L.P. and Wells Capital Management

Wells Fargo Fund	7-day current yield
Cash Investment MMF*–Select	0.35%
Heritage MMF*–Select	0.35%
Municipal Cash Management MMF*–Inst'l	0.10%
Government MMF**–Select	0.11%
Treasury Plus MMF**–Select	0.11%
100% Treasury MMF**–Inst'l	0.05%

Source: Wells Fargo Funds

Figures quoted represent past performance, which is no guarantee of future results, and do not reflect taxes that a shareholder may pay on an investment in a fund. *Yields will fluctuate. Current performance may be lower or higher than the performance data quoted and assumes the reinvestment of dividends and capital gains. Current month-end performance is available at the funds' website, wfam.com.*

Money market funds are sold without a front-end sales charge or contingent deferred sales charge. Other fees and expenses apply to an investment in the fund and are described in the fund's current prospectus.

The manager has contractually committed to certain fee waivers and/or expense reimbursement through May 31, 2021, to cap the funds' total annual fund operating expenses after fee waivers. Brokerage commissions, stamp duty fees, interest, taxes, acquired fund fees and expenses (if any), and extraordinary expenses are excluded from the expense cap. Without these reductions, the seven-day current yield for the Institutional Class of the Cash Investment Money Market Fund, Heritage Money Market Fund, Municipal Cash Management Money Market Fund, Government Money Market Fund, Treasury Plus Money Market Fund, and 100% Treasury Money Market Fund would have been 0.23%, 0.25%, -0.04%, 0.04%, 0.03%, and 0.03%, respectively, and the total returns would have been lower. Prior to or after the commitment expiration date, the cap may be increased or the commitment to maintain the cap may be terminated only with the approval of the Board of Trustees. The expense ratio paid by an investor is the net expense ratio (the total annual fund operating expenses after fee waivers) as stated in the prospectus.

For more information, please contact:

Institutional Sales Desk: **1-888-253-6584**

Website: **wfam.com**

(Click "Select Your Role" in the top navigation and select "Institutional Cash Investor")

1. Variable-rate demand notes (VRDNs) are debt securities commonly held within the Wells Fargo Money Market Funds. Like all bonds, VRDN values fluctuate in response to the financial condition of individual issuers, general market and economic conditions, and changes in interest rates. Changes in market conditions and government policies may lead to periods of heightened volatility in the bond market and reduced liquidity for certain bonds. In general, when interest rates rise, bond values fall and investors may lose principal value. Interest rate changes can be sudden and unpredictable. In addition to credit and interest rate risk, VRDNs are subject to municipal securities risk.

2. A tender option bond (TOB) is a type of VRDN where a long-term bond is placed into a trust. Floating-rate securities are created from the trust.

3. The Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Index is a seven-day high-grade market index composed of tax-exempt variable-rate demand obligations with certain characteristics. The index is calculated and published by Bloomberg. The index is overseen by SIFMA's Municipal Swap Index Committee. You cannot invest directly in an index.

**For floating NAV money market funds: You could lose money by investing in the fund. Because the share price of the fund will fluctuate, when you sell your shares they may be worth more or less than what you originally paid for them. The fund may impose a fee upon sale of your shares or may temporarily suspend your ability to sell shares if the fund's liquidity falls below required minimums because of market conditions or other factors. An investment in the fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. The fund's sponsor has no legal obligation to provide financial support to the fund, and you should not expect that the sponsor will provide financial support to the fund at any time.*

For retail money market funds: You could lose money by investing in the fund. Although the fund seeks to preserve the value of your investment at $1.00 per share, it cannot guarantee it will do so. The fund may impose a fee upon sale of your shares or may temporarily suspend your ability to sell shares if the fund's liquidity falls below required minimums because of market conditions or other factors. An investment in the fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. The fund's sponsor has no legal obligation to provide financial support to the fund, and you should not expect that the sponsor will provide financial support to the fund at any time.

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For the municipal money market funds, a portion of the fund's income may be subject to federal, state, and/or local income taxes or the alternative minimum tax. Any capital gains distributions may be taxable. For the government money market funds, the U.S. government guarantee applies to certain underlying securities and not to shares of the fund

The views expressed and any forward-looking statements are as of June 30, 2020, and are those of the fund managers and the Money Market team at Wells Capital Management, subadvisor to the Wells Fargo Money Market Funds, and Wells Fargo Funds Management, LLC. Discussions of individual securities, the markets generally, or any Wells Fargo Fund are not intended as individual recommendations. Future events or results may vary significantly from those expressed in any forward-looking statements; the views expressed are subject to change at any time in response to changing circumstances in the market. Wells Fargo Asset Management disclaims any obligation to publicly update or revise any views expressed or forward-looking statements.

Carefully consider a fund's investment objectives, risks, charges, and expenses before investing. For a current prospectus and, if available, a summary prospectus, containing this and other information, visit wfam.com. Read it carefully before investing.

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