

European Short-Term Bond Fund Dashboard: January 2022

Varied Approaches under Article 8 SFDR Classification

Over a third of European short-term bond funds (STBFs) are classified under Article 8 of the EU Sustainable Finance Disclosure Regulation (SFDR), based on Fitch Ratings' sample of over 80% of the industry by assets as of end-2021.

Article 8-classified funds claim to promote environmental or social characteristics. Article 6-classified funds, however, which disclose how sustainability risks are incorporated or otherwise deem such considerations as not relevant, were the largest group amongst European STBFs at 47%. Fitch defines STBFs as fixed-income funds with a target duration of one to three years.

Of the STBFs classified under Article 8, Fitch observed different approaches to promoting environmental or social characteristics within the sample. Article 8 funds were equally split between those that assess sustainability risk as a consideration in their investment decisions and those that assess sustainability risk, but in addition explicitly target exposures to companies with the best sustainability practices.

This highlights that, even within a single regulatory classification, sustainability approaches can show meaningful variance. Fitch rates nine funds within the sample, only one of which is classified under Article 8 of the SFDR.

STBFs rated by Fitch maintain a higher credit quality than the industry average, though credit quality for these funds remains weaker than for money market funds (MMFs). Most rated STBFs specify a minimum 'BBB' category rating, versus minimum 'A' or 'F1' category ratings for MMFs.

What to Watch

Data Availability: Market demand for assessments on environmental, social and governance (ESG) impacts should increase as SFDR becomes increasingly referenced by investors. While there has been rapid progress in the availability of data for equities and long-term assets, there are additional complexities faced for short-term assets such as commercial paper.

AUM Growth Sensitivity to Rates: Low or negative rates, combined with higher inflation, have led traditional MMF investors to consider STBFs as part of cash-segmentation strategies, supporting growth in STBF AUM. That said, rate rises in many developed markets are leading to increased MMF yields and may reverse investor allocations to STBFs.

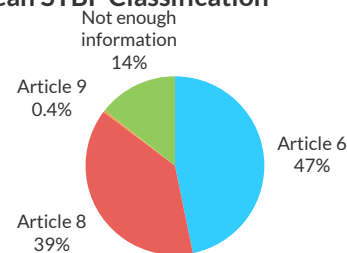


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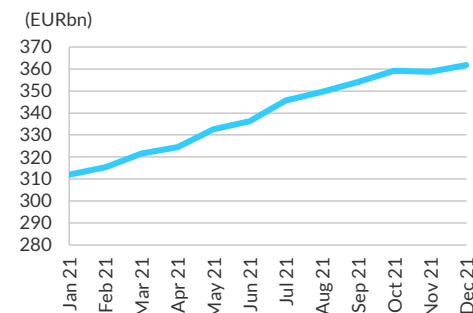
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SFDR Article 6 Most Common European STBF Classification



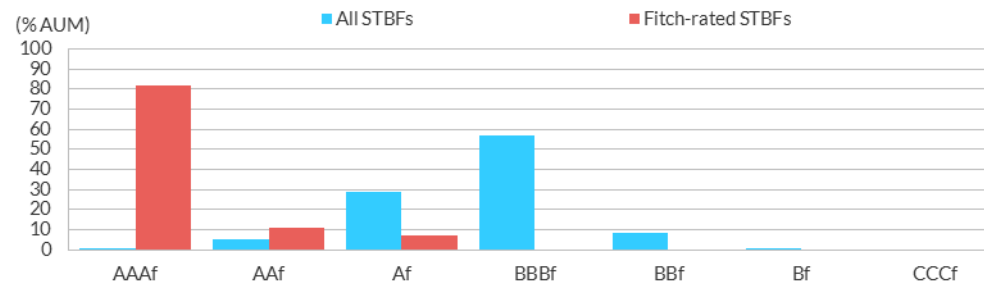
Note: Figures displayed have been rounded
Source: Fitch Ratings and fund documents, Lipper

STBF AUM Growth Steady in 2021



Source: Fitch Ratings, Lipper

Rated STBFs Maintain Higher Credit Quality



Note: Covers approx. 70% of identified STBFs, data as of 31 December 2021
Source: Fitch Ratings, Lipper

SFDR Definitions

Article 6 definition:
Transparency of the integration of sustainability risks
Financial market participants shall disclose how sustainability risks are integrated into investment decisions and the potential impact of those risks on returns
Where financial market participants deem sustainability risks not to be relevant, they shall include a clear and concise explanation of the reasons.

Article 8 definition:
Transparency of the promotion of environmental or social characteristics in pre-contractual disclosures
A fund promotes, among other characteristics, environmental or social characteristics, or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices.

Article 9 definition:
Transparency of sustainable investments in pre-contractual disclosures
A fund has sustainable investment as its objective and an index has been designated as a reference benchmark, the information to be disclosed.

Source: Fitch Ratings

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