European MMF Reform: November 2018 Dashboard

'Decumulating' Share Classes Become Leading Option for Euro LVNAVs

It now appears that reverse distribution mechanisms (RDM) will not be permitted under the European money market fund (MMF) reforms following an extended regulatory debate on this topic. This means euro-denominated low volatility net asset value (LVNAV) funds, if launched, will only be able to offer accumulating share classes, rather than distributing share classes which rely on RDM. RDMs are tools enabling funds to cancel shares, to retain a stable unit value per share where rates are negative. Fitch Ratings forecasts positive eurozone policy rates by end-2019, following which euro LVNAVs with distributing share classes may become feasible. While the fund structure is not necessarily material to our rating analysis, the decision does mean less choice for euro investors compared with other currencies.

About 70% of Conversions Expected in 2018

Fitch expects about 70% of constant net asset value (CNAV) MMFs (by assets under management, AUM) to have converted by end-December 2018 based on dates published. Of this, we expect almost 90% to convert to the new LVNAV fund type. The low percentage (about 12%) converting to the public debt CNAV fund type contrasts with the US MMF reform, in which over USD1 trillion flowed from prime to government funds. European public debt CNAV funds can have a broad range of risk profiles driven by the diverse underlying credit quality of member states.

Standard MMFs Less Affected by Reform

Standard MMFs have, so far, maintained their risk profiles in the run-up to reform. Fitch's review of the largest funds found no obvious trend, suggesting "business as usual" for this segment. However, the reform introduces new minimum liquidity requirements for this fund type and at end-October 2018 average weekly liquidity was 13%, below the new reform requirement of 15%.

What to Watch

Euro CNAV Fund Flows: Much of the over EUR80 billion currently held in euro CNAV fund types may now become spread across LVNAVs with accumulating share classes or convert to alternative fund types, such as short-term variable net asset value funds. Investors unable to accommodate variable share prices may be forced out of MMFs by the RDM decision.

Fund Launches and Conversions: Fitch expects about EUR180 billion equivalent AUM to convert in November 2018, and over 80% of the conversions to be to the LVNAV fund type. Conversion timetables have been affected by the uncertainty around RDMs, with many providers planning or postponing conversion timing to January 2019.

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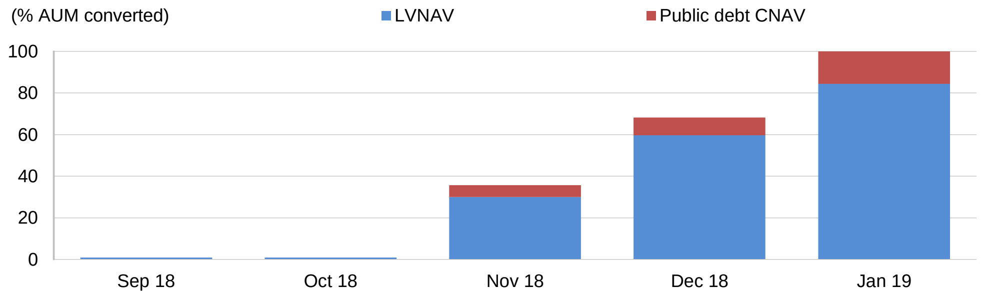
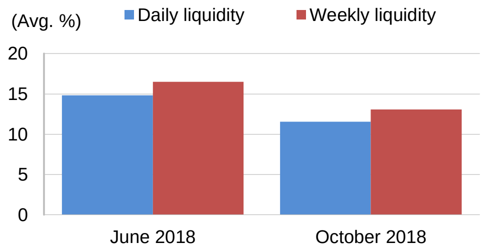
About 70% of Conversions Expected by End-2018



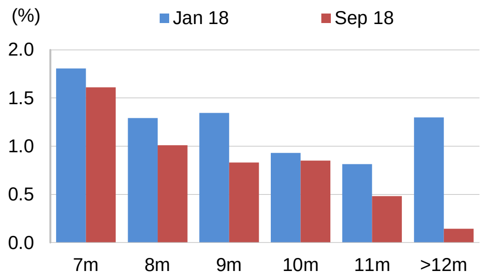
Source: Fitch Ratings, iMoneyNet, MMF managers' websites

Standard MMF Liquidity Lower in Run-Up to Reform



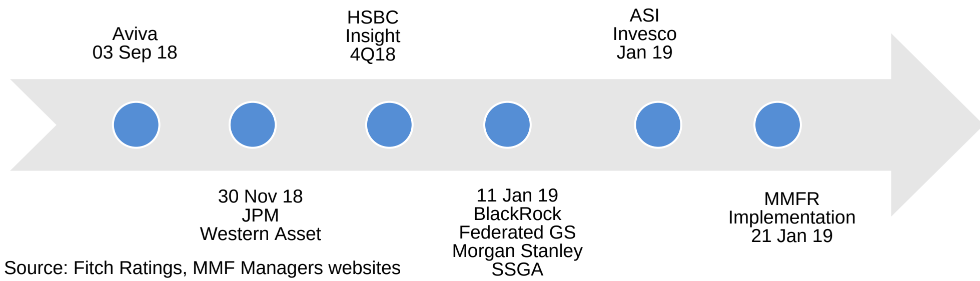
Source: Fitch Ratings, Fund Fact Sheets for standard MMFs with over EUR100 billion AUM

Shorter Maturities in Run-Up to Reform



Source: Fitch Ratings, rated funds

MMF Conversions Timeline



Source: Fitch Ratings, MMF Managers websites