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ICMA
International Capital Market Association

12 July 2016

ICMA

International Capital Market Association

ICMA is the long-established trade association for the international debt capital market. It has over 500 member firms from around 60 countries, including banks, borrowers, asset managers, infrastructure providers and law firms. It performs a crucial central role in the market by providing industry-driven standards and recommendations for issuance, trading and settlement in international fixed income and related instruments. ICMA liaises closely with regulatory and governmental authorities, both at the national and supranational level, to ensure that financial regulation promotes the efficiency and cost effectiveness of the capital market. www.icmagroup.org

Lasting unconventional monetary policies from a capital market standpoint

Foreword by Dr. Nannette Hechler-Fayd'herbe

It has been more than a year now since the ECB and other central banks in Europe embarked on unconventional monetary policy paths with a multitude of collateral implications for their economies, capital flows and exchange rates as well as for capital markets and asset managers. The UK's recent decision to leave the European Union will if anything likely extend the negative interest rate policy and asset purchases (or a combination of the two).

One of the most direct consequences of negative policy rates on the debt capital market is the increase of duration, ie the sensitivity of bond prices to interest rate fluctuations. Leading investment grade benchmark indices for the euro-denominated bond market show an increase in duration of 0.8 years for corporates and even 1.4 years for European sovereigns compared to the last 15-year average. In Switzerland, where negative interest rates are most pronounced, the duration increase is even stronger from 5.5 years on average in the past to 7.5 years now. The higher price sensitivity is relevant for all benchmark-following investors and for retirement schemes that have large shares of fixed income assets. In Europe, it is particularly the case for Germany, where fixed income represents about 50% of pension fund assets. But also Spain, Italy, Austria and the Netherlands are highly exposed to the increase of duration and the resulting risk, once the ECB envisages an exit from its current interest rate policy. Negative interest rates indirectly have an impact on credit spreads too, as they usually lead investors to invest more in credits. This generally results in tighter credit spreads, a positive for corporate issuers who tend to come more to the market, but also in long-term risk if leverage rises. A second implication is a more pronounced buy-and-hold behaviour by investors which in turn leads to wider bid-ask spreads, lower liquidity in the secondary market, over-subscription and more lower quality and even non-rated issuers where this is permissible in the primary market.

Negative interest rates of course go way beyond debt capital markets in their influence. They have been strong drivers of real estate performance and also equity performance, particularly in those sectors that are particularly responsive to interest rates. Utilities, that tend to offer high dividends for example, are strengthened by a negative interest rate environment. Financials that are negatively impacted in their net interest income in contrast tend to underperform in a negative interest rate environment. Also in foreign exchange, negative interest rates act as an important variable, as they tend to restore hedging costs and thereby influence hedging behaviour, an important determinant of demand for currencies.

Asset purchase programmes have some similarities in their impact on the capital market. Falling liquidity in secondary markets, for example, as a result of the crowding-out of private sector investors by central bank purchases, is one such similarity. Credit spread tightening is even more pronounced than in the former case, since this is in general a direct objective of asset purchase programmes that focus on reducing funding costs for corporate issuers. Lower-rated investment grade and speculative credits benefit particularly and become expensive for investors, which have to pay increased attention to credit risk and reward. By impacting credit spreads, asset purchase programmes tend to support risky assets altogether, hence also equities. High beta equities are proportionately more favourably impacted and bank stocks in contrast to the negative interest rate policy regime are better supported.

It is easy to become caught in gloom over the challenges unconventional monetary policies introduce for capital markets and for asset managers and overlook the opportunities. Indeed what better time to consider extensive infrastructure modernization programmes in Europe funded on the debt capital market? The structural challenges faced by a number of European countries certainly cry out for productivity-supporting measures. These include continued investment around transportation, communication, connectivity, resource-efficiency, the development of smart cities etc. Low-debt governments could envisage more dedicated infrastructure-funding without necessarily inducing significantly higher budget deficits due to the low funding costs relieving the system from over-reliance on monetary policy. Innovative alternatives to state-funding such as user-payer models or Build-Operate-Transfers (BOT) could be envisaged too, and add to the European capital market diversity, alleviating the prevailing drought of issuers as compared to the liquidity glut. Reservations towards infrastructure-funding issuers that can be considered as risky due to the budgetary situation would certainly have to be overcome. But the interest for new names and the attractiveness and predictability of the pay-offs such as those provided by such investments speak for these assets.

Dr. Nannette Hechler-Fayd'herbe is Head of Investment Strategy at Credit Suisse, and a Member of the ICMA Board

A message from the Chief Executive

by Martin Scheck

As we all now know, the UK referendum on 23 June 2016 resulted in a vote for the UK to leave the European Union. Capital markets are facing a period of uncertainty while the details of UK withdrawal are worked out. ICMA's focus is as ever on practical measures for ensuring that capital markets can continue to function effectively to benefit all market users and the real economy. To this end ICMA, as a truly international association with around 500 members in 60 countries, will be working actively to support all our member firms as they make complex decisions over the coming months and years, and will be striving to avoid fracture of the European capital market.

The Quarterly Assessment inside this Quarterly Report outlines some of the practical considerations for capital markets following the vote.

ICMA issued the following statement on 24 June:

Following the UK vote on 23 June to leave the EU, ICMA will work actively with all its members, large and small, sell side and buy side, through its Market Practice and Regulatory Policy Committees, Regional Committees and other Working Groups, as appropriate, to help them prepare for the international capital market implications of Brexit. ICMA's mission continues to be the promotion of resilient and well-functioning international capital markets.

ICMA provides standard market documentation and guidance on market practices, which are widely adopted in many areas of the international capital markets. They may potentially need adjustment as the details of the UK's withdrawal from the EU become clearer. ICMA will continue to review its standard market documentation and guidance in the light of future developments and will ensure they are amended as and when needed in consultation with our members.

As the markets adapt to the UK withdrawal from the EU, ICMA will continue to work with the authorities in the UK, the EU, the euro area and elsewhere, to ensure that our members' views in the international capital markets are well represented.

ICMA will keep its members up-to-date with its assessment of relevant new developments: for example, through conference calls, round tables and other events, the ICMA Quarterly Report and the ICMA website. The ICMA Helpdesk and ICMA's staff are available to answer members' questions.

On 24 June, ICMA posted on its website a working document on Brexit: Implications for Capital Market Regulation.

On 28 June, ICMA held a briefing call for ICMA members on the implications for ICMA members of the UK vote to leave the EU.

I can assure you that ICMA's workstreams in all its key areas of market activity with its committees of members are continuing. You will find full reports on progress on primary markets, secondary markets, repo and collateral, green finance and sustainability, and our buy-side work detailed in this edition of the ICMA Quarterly Report.

We launched a new study at the beginning of July, entitled *Remaking the Corporate Bond Market*. This is ICMA's second study into the state and evolution of the European investment grade corporate bond secondary market and is based on an extensive series of interviews with market participants – issuers, intermediaries, investors and infrastructure providers – and, where quantitative data is available, we have also considered this in drawing conclusions. Although the research was done prior to the UK referendum, the findings and conclusions of this study have become even more relevant, as we enter a period of even greater economic uncertainty, and when market efficiency and liquidity will, potentially, be sorely tested.

On a slightly different note, I would like to thank those of you who came to ICMA's 48th AGM and Conference in Dublin at the end of May. We had a record turnout of close on 1,000 delegates in total. A fuller write-up and photos of the conference appear on our website and in the events section of this Quarterly Report.

Martin Scheck
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The UK vote to leave the EU: implications for capital market regulation

Quarterly Assessment by Paul Richards

Introduction

1 As a result of the UK vote in the EU referendum on 23 June to leave the EU, there is considerable uncertainty in capital markets about the implications. The purpose of this Quarterly Assessment is to focus on the implications of the UK vote to leave (ie Brexit) for capital market regulation.[1] It does not cover the wider political and economic implications of the UK vote to leave. HM Treasury and the Bank of England, the IMF and the OECD, among others, have already set out their assessments of the potential impact of the UK vote to leave on UK economic growth and inflation, the sterling exchange rate, UK interest rates, the UK's credit rating, the stability of the UK financial system, foreign direct investment and employment in the UK, both in the near term and the longer term; and they have also set out their assessments of the potential economic impact on the rest of the EU, as the UK's main export market.

Stage 1: Notification of withdrawal

2 The first formal step towards withdrawal from the EU is for the UK Government to notify the European Council of the UK's intention to withdraw by invoking Article 50 of the EU Treaty. Invoking Article 50 is considered to be the only legal way to leave the EU. It is for the UK Government to decide when to invoke Article 50, subject to majority support in Parliament. The Heads of Government of the remaining 27 EU Member States stated at their meeting on 29 June that the UK should notify the European Council as quickly as possible, and that "there can be no negotiations of any kind before this notification has taken place".

3 Article 50 has not previously been tested, but it should provide a period of up to two years for the UK Government to negotiate withdrawal from the EU with the European Council, acting by enhanced qualified majority voting (QMV) with the consent of the European Parliament.[2] If no agreement is reached, the UK will leave the EU two years after Article 50 is invoked, unless there is unanimity among the other 27 EU Member States on extending the negotiations beyond two years.

4 A second referendum has been ruled out by the UK Government. It is not clear whether this would necessarily bind a future Government. A second referendum might in theory be called, for example, at the end of the withdrawal negotiations once the settlement terms for the UK have become clear; and the settlement terms would in any case need to be approved in the UK by Parliament. There are precedents for second referenda in the cases of Denmark and Ireland. But these referenda concerned EU Treaty changes. They did not involve withdrawal from the EU under Article 50. Once Article 50 has been invoked, it is not clear whether it would be possible for the UK to stop the Article 50 process before withdrawal if the UK subsequently decided to remain in the EU.

5 EU legislation – including new EU laws – will continue in effect in the UK until withdrawal. But following the vote in the UK to leave the EU, it is not clear what would happen if the primacy of EU legislation in the UK were to be challenged in some way before UK withdrawal.[3]

6 The safeguards negotiated by the UK Government with the European Council on 19 February, if the UK voted to remain in the EU, will not apply now that the UK has voted to leave.[4]

> Invoking Article 50 is considered to be the only legal way to leave the EU.

1. This paper updates the previous Quarterly Assessment on: Brexit: Practical Implications for Capital Markets (April 2016).

2. Qualified majority voting: at least 55% of EU Member States representing at least 65% of the total EU population. Enhanced qualified majority voting: at least 72% of EU Member States representing 65% of the EU population.

3. eg by limiting in the UK the powers of the European Court of Justice or restricting free movement of people into the UK from the rest of the EU.

4. Decision of Heads of State or Government, meeting within the European Council, concerning a New Settlement for the United Kingdom within the European Union, 19 February 2016.

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It is not yet clear which approach the UK Government will adopt, nor what the EU response will be.

Stage 2: Withdrawal negotiations

(i) Withdrawal options for the UK

7 During the negotiations on withdrawal[5], the UK Government is expected to seek a new agreement on UK/EU relations in future. In the negotiations on a new agreement, the main question affecting capital markets will be the terms of future UK access to the EU Single Market, given that the UK currently has unrestricted free access through the "single passport"[6] as a member of the EU, and that unrestricted free access to the EU Single Market will cease on the UK's withdrawal unless there are new arrangements to replace it.

8 In its assessment in March 2016 of possible models for the UK outside the EU, HM Treasury considered three main withdrawal options[7]:

- *Leave the EU and join the European Economic Area (EEA):* Under this option, the UK would apply to join EFTA as a means of joining the EEA (like Norway).[8] As a result, the UK would continue to have unrestricted free access to the EU Single Market through the single passport. But the UK would not have a vote on new EU legislation in future and would need to continue complying with EU financial regulation under the jurisdiction of the European Court of Justice, accepting the free movement of people from the EU and making a contribution to the EU budget.
- *Leave the EU and negotiate a bilateral trade agreement:* Under this option, the UK would negotiate a bilateral agreement with the EU (like Canada).[9] The negotiation of the Canadian agreement with the EU (CETA) has so far taken seven years, and it still needs to be ratified by all 28 EU Member States and the European Parliament. Once ratified, CETA will allow substantial access to the EU Single Market for most goods, but will not provide a single passport for financial services.
- *Leave the EU and trade under World Trade Organisation (WTO) rules*, including trade in services through the General Agreement on Trade in Services (GATS): This option would not require prior agreement by the UK with the rest of the EU, nor involve the implementation of EU regulations, nor acceptance of the free movement of people from the EU, nor making a budgetary contribution to the EU. But it would not give preferential access to the EU Single Market. Instead, it would mean that UK exports both to the EU and other WTO members would be subject to the same WTO tariffs; and, in the case of services, the EU would only be obliged to give a much more basic framework under GATS than the EU Single Market, and much less favourable access.[10]

(ii) UK withdrawal negotiations with the EU

9 It is not yet clear which approach the UK Government will adopt, nor what the EU response will be. If the UK wanted to obtain the most favourable terms of access to the EU Single Market, this would mean complying with EU legislation, both at the outset and on a continuing basis in future; continuing to permit free movement of people between the UK and the rest of the EU; and continuing also to make a contribution to the EU budget. It has been reported that there might be a majority in the House of Commons in favour of retaining unrestricted free access to the EU Single Market through the single passport as the best way of implementing the vote by the British people in the referendum to leave the EU.

10 However, it appears that the priority for the UK campaign to leave the EU (the "Brexit campaign") is to ensure that, after the UK withdraws, the UK will not be subject to the European Court of Justice and that the UK can control EU immigration. It is not clear whether the UK vote to leave the EU will be interpreted by the UK Government as a vote to give priority to these objectives, even if this means leaving the EU Single Market, which

5. eg the terms of withdrawal from the UK's budgetary commitments to the EU.

6. The "single passport" allows financial services operators legally established in one EU Member State to establish or provide their services in the other Member States without further authorisation requirements.

7. HM Treasury: Alternatives to Membership: Possible Models for the UK outside the EU (March 2016).

8. It is possible that the idea of an "association agreement" between the UK and the EU would be a variation on the Norwegian option, though that is not yet clear.

9. Switzerland has 120 bilateral agreements with the EU. But the EU is not thought to favour this model, particularly since 2014 when Switzerland voted to restrict EU immigration.

10. The previous Secretary General of the WTO warned in May that "the WTO would be a terrible replacement for access to the EU Single Market", and that "there has not been a major WTO deal in 23 years": Pascal Lamy: Britain Won't Get Better Trade Deals if it Leaves Europe: The Times, 3 May 2016.

The EU would be expected to argue that, as a condition for future access to the EU Single Market on favourable terms, UK law should continue to conform in future with EU law.

comes under the jurisdiction of the European Court of Justice and requires the free movement of people within the EU. But the Heads of Government of the remaining 27 EU Member States said at their meeting on 29 June that "access to the Single Market requires acceptance of all four freedoms" (ie including the freedom of movement of people within the EU).

11 Under those circumstances, negotiating a Canadian-style trade agreement with the EU would be one option for the UK. But, in addition to the complexity of the issues at stake, any UK trade deal with the EU would have to be ratified by all the other 27 EU Member States and the European Parliament. The President of the European Council has estimated that negotiating and ratifying such an agreement might take up to seven years[11]. If so, it might be necessary – should the UK leave the EU in the meantime[12] – for the UK to trade under WTO rules for a period. But that might not be necessary if the negotiations could be completed by 2020 (ie the currently scheduled date for the next General Election in the UK), as the Brexit campaign hopes. If the UK adopted this approach, it is not yet clear what would happen in the case of UK financial services.

12 To leave the EU, UK legislation will need to be changed, in particular by repealing the UK European Communities Act 1972. In the case of the capital markets, the regulations affecting the UK at present are largely set at EU level. EU regulations take the form of Directives, which have to be transposed into UK law[13], and Regulations, which apply directly in UK law without transposition:

- Although EU Directives have been transposed into UK law, the UK Government will need to take decisions about whether to keep, modify or discard them. For example, how will MiFID II, which is due to be implemented on 3 January 2018, be handled?
- As EU Regulations apply directly in the UK, they will cease to apply once the UK European Communities Act 1972 has been repealed. The question will then arise whether to replace them, and if so on what basis. This would be the case, for example, with MiFIR.
- These issues relate not only to EU legislation at Level 1, but to Regulatory and Implementing Technical Standards at Level 2 under the auspices of the European Supervisory Authorities (ESAs). In addition, Credit Rating Agencies in the UK are directly supervised by ESMA. It is not clear what future arrangements there will be between the ESAs and the UK.

13 There is likely to be a better chance of gaining favourable terms of access to the EU Single Market, after the UK leaves, if existing EU legislation is "grandfathered": ie Directives already transposed into UK law are left unchanged; and Regulations which will no longer apply directly in the UK once the UK European Communities Act 1972 is repealed are replicated under UK law. This would make it easier for the UK to argue that, when it withdraws from the EU, UK legislation is equivalent to the EU at the outset, so that the UK can obtain favourable access to the EU Single Market as a result. It assumes that the UK would be willing to grant cross-border access to the EU on a reciprocal basis. Some EU legislation (eg MiFID II) provides that the EU can deem third country regimes to be equivalent in exchange for reciprocity, though that does not apply in all cases, and in the case of MiFID II it depends on a judgment by ESMA.

14 The EU would be expected to argue that, as a condition for future access to the EU Single Market on favourable terms, UK law should continue to conform in future with EU law under the European Court of Justice. And the EU may also set, as a condition, that the free movement of people between the UK and the EU should continue.[14] It is not clear whether this would be politically acceptable in the UK. On the one side, the Brexit campaign in the UK has argued against meeting these conditions. On the other side, there might be a majority in the House of Commons for staying in the EU Single Market as the best way of implementing the vote by the British people to leave the EU. Whatever the eventual outcome, there will be uncertainty about the outcome until the withdrawal negotiations with the rest of the EU are complete: ie for two years or longer.

11. The House of Lords European Committee has estimated that an agreement between the UK and the EU would take between four and nine years to complete. The Former Secretary General of the WTO has estimated that it would take between five and fifteen years.

12. eg if there is not unanimity under Article 50 on extending the negotiating period beyond two years.

13. ie English and Scottish law.

14. However, in the case of the 2014 agreement between the EU and the Ukraine, there are restrictions on free movement of people.

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It is by no means clear that leaving the EU will lead to less capital markets regulation in the UK than would otherwise be the case.

(iii) UK negotiations with the rest of the world

15 As trade agreements between the EU and the rest of the world are an EU rather than national competence, new agreements will need to be negotiated between the UK and 53 other markets in the rest of the world, unless the UK is going to trade solely under WTO rules. It needs to be established to what extent negotiations can begin immediately or whether the UK's largest trading partners (eg the US and China) will insist on waiting for an EU agreement first. There is also a question about how long these agreements will take to negotiate.[15] During his visit to London in April, President Obama said that, if the UK voted to leave the EU, a UK/US trade deal would be at the back of the queue, and could take five to ten years. As the UK has not been directly involved in trade negotiations for over 40 years, the UK will also need to train officials or hire experts to conduct them. In the meantime, after withdrawal from the EU, UK trade with the rest of the world would be subject to WTO rules.

Stage 3: Post-withdrawal

(i) Implications for capital market regulation in the UK

16 It is by no means clear that leaving the EU will lead to less capital markets regulation in the UK than would otherwise be the case, for three main reasons:

- *Global level:* While the detailed regulations affecting capital markets in the UK are set at EU level, the overall framework for capital markets regulation is set at global level by the G20, working through the FSB, BCBS and IOSCO. The UK participates in the G20, and will need to continue meeting these global standards, even though it has voted to leave the EU.
- *EU level:* The UK will need to continue complying with the terms of EU regulations, if it wants to obtain favourable terms of access to the EU Single Market after leaving the EU. In the case of capital market regulation, that would be expected to include the CRD, the Prospectus Regulation, the Market Abuse Regulation, MiFID II/MiFIR, Solvency II, UCITS, AIFMD and EMIR, among others.
- *National level:* Since the international financial crisis, the national regulators in the UK – the PRA and FCA – have been among the most prominent national regulators in promoting strict regulation, as the FSA was before them.

(ii) Implications for UK relations with EU and euro-area institutions

17 The withdrawal of the UK from the EU will affect the capital market relationship between the UK and the European authorities in a number of other ways. For example:

- The EU's project for Capital Markets Union, promoted by the European Commission, is likely to be affected. There is a risk that the UK vote to leave the EU will fragment capital markets in the EU between London as an international financial centre and the rest of the EU, particularly if the UK is no longer a member of the EU Single Market after withdrawal. The UK's vote to leave has also led to the resignation of Lord Hill, the European Commissioner for Financial Stability, Financial Services and Capital Markets Union.
- The European Central Bank may take a different approach to counterparties in London with the objective of drawing euro markets from London into the euro area. For example, will access to the euro payments system be affected by the UK vote to leave the EU? And will central counterparty clearing move inside the euro area in order to obtain better access to liquidity from the ECB, as the ECB will no longer need to treat London-based activities as part of the EU?
- UK membership of other EU institutions involved in the capital markets will be affected. For example, after withdrawal, the UK may no longer qualify to be a full member of the European Investment Bank; the European Banking Authority, which is currently based in London, may decide to move its headquarters to a centre within the euro area; and it is not clear whether the proposed London Stock Exchange/Deutsche Börse merger will be permitted to have headquarters in London, if the merger goes ahead.

15. "It is probable that it would take an extended period to negotiate first our exit from the EU, secondly our future arrangements with the EU, and thirdly our trade deals with countries outside the EU, on any terms that would be acceptable to the UK. In short, a vote to leave the EU would be the start, not the end, of a process. It could lead to up to a decade or more of uncertainty.": HM Treasury: The Process for Withdrawing from the European Union (February 2016).

- There is also a question whether UK law will be used in EU financial contracts as much in future, and whether the EU and euro-area institutions will encourage the use of alternatives, and if so which these will be.

(iii) Implications for the EU

18 Aside from the impact on the UK economy, the UK decision to leave will have an impact on the economy of the EU; and there may be a political risk of contagion which results in referenda in some other EU Member States. So remaining EU Member States are not expected to respond during the withdrawal negotiations by granting favourable terms to the UK. It is also possible that the rest of the EU may react to the UK's withdrawal by proposing closer economic integration of the euro area and more cooperation on security and defence.

19 As the New Settlement for the UK agreed with the European Council on 19 February 2016 would only have applied if the UK had voted to remain in the EU, the New Settlement will not apply, since the UK has voted to leave. The New Settlement would have provided safeguards against discrimination between the euro area and the rest of the EU. So the absence of these safeguards may have implications, not only for the UK, but also for other non-euro area Member States, particularly those such as Sweden and Denmark not considering whether to join the euro area. Without the UK, the EU and the euro area could gradually become more synonymous.

(iv) Implications for the future of the United Kingdom

20 As the UK as a whole has voted to leave the EU, but Scotland has voted to remain, there will be uncertainty in capital markets about whether Scotland will in due course hold a second referendum (after the referendum in September 2014) on leaving the UK, with a view either to remaining in the EU when the UK leaves or, if that is not possible, applying as an independent country to rejoin the EU. In the case of Northern Ireland, the border between the North and South of Ireland is currently the UK's only land border with the rest of the EU. So the question will be whether the border should be controlled, and if so, how.

Business planning for Brexit

21 Planning for Brexit by financial institutions involved in the capital markets – both in the UK and outside the UK in relation to their UK counterparties – is still difficult because of uncertainty about the outcome of the negotiations between the UK and the EU and uncertainty about the length of time before the outcome becomes clear. But financial institutions' planning is likely to include, *inter alia:*

> **Planning for Brexit is still difficult because of uncertainty about the outcome of the negotiations between the UK and the EU and uncertainty about the length of time before the outcome becomes clear.**

- *taking steps to ensure their continued financial stability*: eg by checking the impact of Brexit on their capital adequacy, their liquidity and their access to funding against market volatility and the risk of capital flight;
- *setting out the risks of Brexit to their businesses*: eg in their annual reports; and considering whether a risk factor relating to Brexit needs to be included, in the event that they issue a prospectus;
- *checking whether their financial contracts will be affected*: eg to take account of changes in UK legislation after Brexit;
- *reviewing their future investment plans*: the UK will not be as attractive a location for access to the EU Single Market as it has been in the past as part of the EU Single Market, given the UK vote to leave the EU;[16]
- *reviewing their future staff location plans*: if EU citizens required permission to work in the UK in future, UK citizens would be expected to require permission in future to work in the EU; and
- *considering the time needed to make any changes*: in the case of any financial institution that decides to relocate some of its capital market activities and staff as a result of setting up subsidiaries in the rest of the EU to obtain passport-free access to the EU Single Market, planning such a transfer is likely to take time, and plans may need to be put into effect before the outcome of the UK's new trading relationship with the EU is known.

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16. "Over 5,000 firms, including banks, investment firms and insurance companies, hold passports which enable them to provide their financial services and establish branches in other EU Member States.": FCA evidence to the Treasury Select Committee: 3 February 2016.

Remaking the corporate bond market

By Andy Hill

Summary

ICMA's 2nd study into the state and evolution of the European investment grade corporate bond secondary market, *Remaking the Corporate Bond Market,* sets out to explore how the European investment grade corporate bond market has developed since ICMA's 2014 study on the state and evolution of this market. It reviews how liquidity and market efficiency are being defined and impacted by the confluence of extraordinary monetary policy and unprecedented prudential and market regulation, and what the implications for the market are. Unlike the previous report, which was largely based on a series of in-depth interviews with market participants represented by ICMA – investors, issuers, banks and broker-dealers, intermediaries and infrastructure providers – this report relies on both qualitative and quantitative input from these market participants. It also asks where the market is heading, what are the challenges and opportunities in front of us, and provides recommendations to support the long-term efficiency and functioning of the market.

Corporate bond markets serve a vital economic function of bringing together corporations requiring capital to fund or expand their businesses and investors and savers looking to earn a stable income from their investments and savings. They thus play a key role in facilitating economic growth, productivity, and employment. As the ability of banks to provide direct funding to the corporate sector has become challenged, post-crisis, policy makers are beginning to look to capital markets as an ever more important source of financing for the real economy, while also underpinning economic stability; an objective that is at the very heart of Europe's plan to build a Capital Markets Union.

Since ICMA published its report in 2014, the discourse around bond market liquidity, and its potential implications, has entered the mainstream when it comes to assessing market risks or explaining market behaviour. A number of market and academic studies have explored further the theme of bond market liquidity, across a range of asset classes, including investment grade corporate bond markets. The conclusions, based on various data collection exercises, have been mixed, with most market studies suggesting that market conditions, in general, are becoming more challenged, while a number of more academic-based studies published by authorities and regulators tend to be more sanguine. Understanding the reasons for this apparent divergence of perspectives is one of the motivations for this second study.

Market participants report that in the current environment it continues to be more challenging both to provide and source liquidity, primarily as the result of the concurrence and interaction of various regulatory initiatives and extraordinary current and future monetary policy, and the undermining of the market-making liquidity model, largely due to greater capital constraints on banks and broker-dealers. It appears to be increasingly difficult to trade in large sizes, to execute orders quickly, or to establish reliable prices. European corporate issuers are also increasingly concerned about the state of the corporate bond secondary market, which directly impacts their ability to raise capital necessary to fund investment. They note an unsustainable disconnect between primary market stability and secondary market liquidity that is being perpetuated primarily as the result of ongoing central bank intervention.

However, since the 2014 study, market participants are more resolved to adapt to the new norm, and are evolving their business models accordingly. While sell-side firms continue to reshape their models around balance sheet efficiency, acting more as principal brokers than market-makers, the buy-side is taking more initiative in terms of locating and creating liquidity. While technology is playing an increasingly important role in the market, there is growing recognition that a significant part of the market will always need to be "people-based", and so values such as trust and relationship building are becoming ever more important as market conditions becomes more challenged.

There is an evolving sense that the whole market architecture may need to be redesigned if it is to continue to support its essential function of facilitating investment in the real economy. This will require the close cooperation of all market stakeholders, including issuers, asset managers and investors, banks and intermediaries, infrastructure providers, as well as policy makers and regulators. Given the breadth and diversity of its membership across the European region, ICMA is perfectly placed to bring all these key actors together.

Conclusions

This latest study provides four key observations.

First, for the most part, *the ability either to source or provide secondary market liquidity continues to be challenged*. The interviews, survey, and data, in general, point to a market where it is becoming increasingly difficult to trade in large sizes, to execute orders quickly, or to establish reliable prices. Furthermore, the difference in ease of access to liquidity available to the largest buy-side firms, compared with their smaller competitors, appears to be widening. The principal factor underlying this remains the reduced capacity of the sell-side to make markets, primarily due to higher capital costs and less functional hedging and financing markets. The low-rate, spread-compressed environment only adds to the reasons for retracting the provision of liquidity.

Second*, despite a more challenged environment, the general mood of most market stakeholders compared to 2014 is significantly more upbeat*. Sell-side firms are reinventing themselves as more client-focused principal brokers, selectively providing balance sheet where it makes sense, and relying more on data management to facilitate what is becoming an axe-driven, rather than quote-driven, market. Correspondingly, the buy side is realizing that they can no longer rely unconditionally on their broker-dealers, and increasingly and proactively are establishing themselves as part of the liquidity creation equation. They, too, are becoming more discerning about who they deal with, expanding their broker relationships, utilizing data to identify more efficiently which brokers are more likely to have an interest, and expanding their potential counterparties to other buy-side firms. Meanwhile, platform providers and intermediaries, both established incumbents and adventurous newcomers, are busily innovating and attempting to provide new tools and protocols to help bridge the liquidity gap.

The third key observation is that, *compared with the 2014 interviews, the corporates themselves are becoming increasingly concerned by, and engaged in, the discussions around secondary market liquidity.* There seems to be a recognition of a growing disconnect between primary market stability and secondary market liquidity; something that would be unsustainable under normal market conditions, but is being ensconced by extraordinary monetary policy. What becomes clear from the latest study is that, while the issuers may have little direct involvement in, or limited scope to affect, the secondary market, they are more eager than ever to be part of the discussion to find a solution. They, more than anyone, have the most to lose from a dysfunctional secondary market; along with the people they employ, and the economic activity they help to sustain.

> **The current market model is not sustainable, at least not in the long term, and certainly not post central bank intervention.**

Finally, and a key message that comes through in the recent interviews is that, *from the perspective of many participants, the current market model is not sustainable, at least not in the long term, and certainly not post central bank intervention.* At a time when Europe's leaders are looking to develop and expand its capital markets as a means to support economic growth and diversity, the capacity to sustain liquidity in those markets is being simultaneously undermined. As a number of participants in this study were keen to express, there is a pressing need to review the prevailing market model, and possibly to redesign how this can work going forward. Particularly in light of the increasing constraints and limitations on its participants, not least those who are the principal source of market liquidity. Furthermore, this cannot be done in isolation, and will require the cooperation and collaboration of all market stakeholders, including investors and asset managers, corporate issuers, banks and broker dealers, intermediaries and infrastructure providers, the relevant market associations and representative bodies, as well as policy makers and regulators.

In short, it might be time that we all need to begin rethinking, and possibly "remaking", the European corporate bond secondary market.

Recommendations

Based on the stakeholder interviews underlying this survey, there are a number of possible measures that could be taken, either in isolation or in combination, in order to improve the long-term efficiency and functioning of the European corporate bond markets.

- *Provide capital relief for market-making.* Given the

> **All market stakeholders need to work together in a formalized and structured forum to share views and ideas on market structure and development.**

heterogeneous and inherently illiquid nature of credit markets, the market-making model is the optimal, and perhaps the only viable, source of true market liquidity. While there are multiple pressures on banks and broker-dealers' capacity or willingness to provide market-making services in bond markets, it becomes clear that the increased cost of capital is perhaps the single biggest constraint. Given the economically important and socially useful service that market-makers provide in supporting the efficiency and functioning of corporate bond markets, policy makers and regulators should at the very least consider the possibility for less stringent capital charges related to this activity, including associated hedging and financing.

- *Revitalize the single-name CDS market.* Single-name CDS not only provide an efficient and standardized tool for market-makers and investors to hedge credit exposures, but given its close relationship with the underlying reference bonds, an active and liquid single-name CDS market could help stimulate liquidity in the corporate bond market. Measures to revitalize the market could include reviewing CVA capital charges and NSFR funding requirements under CRD IV/R.
- *Review and reassess harmful regulation*. It becomes clear that there are a number of regulatory initiatives that seem to offer no obvious benefits to fixed income markets, and, in certain cases, are likely to cause significant harm. There is a strong case for suspending the projected implementation of these regulatory initiatives with a view to undertaking rigorous and detailed impact analyses. Chief among these would be MiFID II/R pre-trade transparency obligations for bonds and CSDR mandatory buy-ins.
- *Bring all market stakeholders together to review the market structure*. All market stakeholders, including investors and asset managers, corporate issuers, banks and broker dealers, intermediaries and infrastructure providers, relevant market associations and representative bodies, as well as policy makers and regulators, need to work together in a formalized and structured forum to share views and ideas on market structure and development. Only through a greater understanding and appreciation of different stakeholder needs and perspectives can the market community achieve consensus and develop private and public initiatives to maintain and grow a healthy and vibrant pan-European corporate bond market.

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ICE Data Services Liquidity Tracker

ICE Data Services has established a means of tracking liquidity conditions in fixed income markets, in response to a request from ICMA.

ICE Data Services Liquidity Indicators

The model is based on ICE Data Services' Liquidity Indicators, which are designed to provide an independent view of near-term relative liquidity, defined as "the ability to exit a position at or near the current value." The indicators use a transparent methodology to assign a liquidity ratio to an individual security, based on the interaction between projected price volatility and trade volume capacities.

ICE Data Services provide estimates of trade volume capacity, future price volatility, days to liquidate, and market price impact. Liquidity ratios for all securities are ranked from least liquid to most liquid, and scored between 0 and 10 (with 10 being the most liquid). These scores, based on ICE Data Services' extensive evaluation and reference data, are updated daily.

ICE Data Services Liquidity Tracker

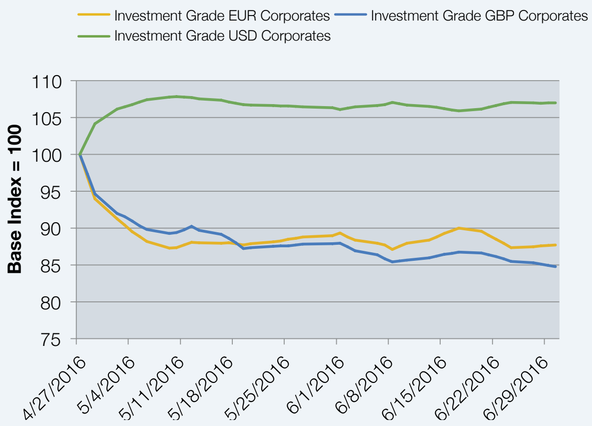
The ICE Data Services Liquidity Tracker is based on the average liquidity ratios of an extensive basket of securities for each market segment. The number of underlying ISINs used to calculate the tracker are: IG USD 15,742; IG EUR 2,828; IG GBP 672; HY USD 12,217; HY EUR 1,865; HY GBP 423. Investment grade is determined by a minimum BBB- rating from one of the three main rating agencies, and includes financials and non-financials.

The starting reference point for the tracker is 27 April 2016, where it is assigned a value of 100. Data is then run on a look-back basis to determine relative changes in market liquidity since the reference date. To ensure continuity in the data series, only issues active at the reference date are included in the ICE Data Services Liquidity Tracker.

Using the Tracker

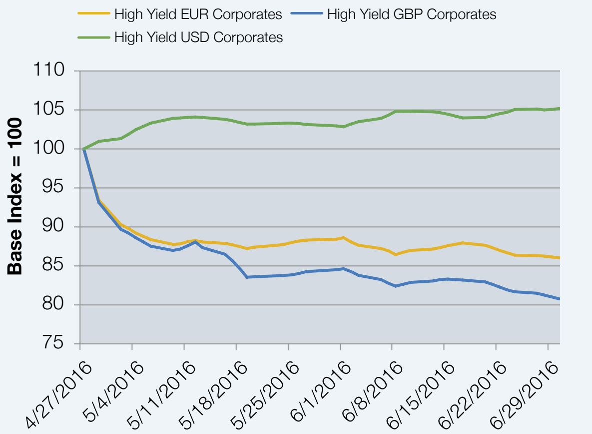
With the permission of ICE Data Services, ICMA intends to publish and monitor the ICE Data Services Liquidity Tracker on a quarterly basis. There is also the possibility of extending the ICE Data Services Liquidity Tracker to other asset classes, including sovereign bonds, as well as creating a more granular sector-based tracker.

ICE Data Services Liquidity Tracker: IG Corporates



Source: ICE Data Services

ICE Data Services Liquidity Tracker: IG Corporates



Source: ICE Data Services

Declining liquidity since the end of April

While the ICE Data Services Liquidity Tracker only goes back as far 27 April 2016, perhaps not too much should be inferred from this relatively short time series. However, the marked drop in euro and sterling corporate bond market liquidity, both for investment grade and high yield, is consistent with anecdotal reports of markets becoming less liquid in the run-up to the UK referendum, and being even less so in the immediate aftermath.

Disclaimer: The ICE Data Services Liquidity Tracker is provided for information purposes only. While the data is taken from sources believed to be reliable, ICE Data Services and ICMA do not represent or warrant that it is accurate or complete, and neither ICE Data Services nor ICMA shall have any liability arising from or relating to the use of the ICE Data Services Liquidity Tracker.

2016 update of the Green Bond Principles

By Nicholas Pfaff and Valérie Guillaumin

The Green Bond Principles (GBP) held their second Annual General Meeting (AGM) in London on 16 June 2016 hosted by the European Bank for Reconstruction and Development (EBRD). The GBP AGM was followed by the second annual GBP conference also held at the EBRD and open to all GBP stakeholders and the press. The key focus of both events was the 2016 update of the GBP.

The GBP are self-regulatory guidelines that provide the framework for the development of the Green Bond market based on transparency and disclosure. The GBP are recognised by a community of almost 200 investors, issuers, underwriters and observers globally, as well as increasingly by the official sector, as the reference for best practice both in developed and developing markets. ICMA runs the Secretariat of the GBP.

Green Bonds raise funds for new and existing projects with environmentally sustainable benefits. The Green Bond market has grown substantially in recent years, with issuance at mid-2016 of US$35 billion (representing already over 80% of 2015 total issuance), from a wide variety of corporates, banks, multilateral development institutions, government agencies, as well as regional and municipal issuers.

The 2016 edition of the GBP benefits from the input of GBP members and observers, from working groups and the wider Green Bond stakeholder community, and also takes into account recent market developments. While the 2016 update continues to be framed by the same four core components (use of proceeds, process for project evaluation and selection, management of proceeds and reporting), a particular effort was made to recommend best practice on reporting and external reviews, including the use of templates designed to be made available publicly to the market through a GBP Resource Centre hosted by ICMA. It is expected that this will add significantly to market transparency and clarify further the process of Green Bond issuer alignment with the GBP.

Highlights of the GBP 2016 Update

- ✓ Recommended public disclosure of Green Bond issuer alignment with the GBP through online GBP Resource Centre
- ✓ Updated and additional Green Project categories
- ✓ Clarifications on Green Bond issuer reporting obligations and disclosure, as well as new resources for impact reporting
- ✓ External review definitions and public disclosure on the online GBP Resource Centre
- ✓ Definition of Green Bonds vs pure play and climate/green themed bonds
- ✓ Release of Guidelines for Social Bond issuers

“A particular effort was made to recommend best practice on reporting and external reviews, including the use of templates designed to be made publicly available on a GBP Resource Centre hosted by ICMA.

The update contains new definitions and guidance for the type of external reviews that issuers are recommended to use to demonstrate their environmental project selection processes and their adherence to GBP recommendations. Further additions and details have also been included on green categories to help issuers and investors identify eligible green projects. Reporting recommendations have generally been strengthened and include important clarifications for issuers on ongoing expectations, and point to resources for impact reporting. Reference is also now made to the wider universe of environmental and climate themed bonds, including those from "pure play" green companies, to distinguish them from Green Bonds while also suggesting the adoption of GBP best practice where possible.

This update of the GBP acknowledges the application of the "use of proceeds" bond concept to themes beyond the environment, such as bonds financing projects with social objectives, or with a combination of social and environmental objectives. *Guidance for Issuers of Social Bonds* has therefore been developed in conformity with the core components of the GBP, providing voluntary guidelines facilitating transparency and disclosure in this emerging segment.

The GBP 2016 update was coordinated, with the support of the ICMA Secretariat, by the Executive Committee of the GBP, a representative group of 24 key market participants, divided equally between issuers, investors and intermediaries. In line with GBP governance, 50% of the seats of the Executive Committee were up for renewal at the AGM. Following a prior e-mail ballot in which 66% of GBP members participated, the majority of the related organisations were reelected, with BNPP and NIB joining as new members.

GBP Executive Committee as of June 2016		
Investors	**Issuers**	**Underwriters**
ACTIAM	EBRD	BoA MERRILL LYNCH
BLACKROCK	EIB	BNP PARIBAS
CalSTRS	ENGIE	CREDIT AGRICOLE CIB
KFW	IFC	HSBC
MIROVA	NIB	JP MORGAN
STANDISH MELLON AM	UNIBAIL-RODAMCO	MORGAN STANLEY
TIAA-CREF	UNILEVER	RABOBANK
ZURICH ASSURANCE GROUP	WORLD BANK	SEB

Note: GBP Executive Committee members in blue elected for a new 2-year term; the term of those in black ends in 2017.

The GBP AGM was also the opportunity to highlight some of the key activities of the GBP during the last 12 months such as:

- the GBP involvement in the official COP21 session on private sector finance and the joint organization of a roundtable with the OECD and other partners;
- ICMA's role on behalf of the GBP in the G20's Green Finance Study Group (GFSG) coordinated by the People's Bank of China (PBOC) and the Bank of England;
- ICMA's participation in China's Green Finance Committee under the auspices of the PBOC with the subsequent release of the PBOC's Green Bond rules and the Green Bond Project Catalogue (2015 Edition);
- input into the Securities and Exchange Board of India's green bond recommendations in the Indian market;
- responses to the EU's study on the *Potential of the Bonds Market for Resource Efficiency Finance,* focusing on the Green Bond market;
- ICMA's participation in the City of London's Green Finance Initiative.

The afternoon conference that followed the GBP AGM attracted nearly 300 participants and confirmed its role as the landmark annual conference for the Green Bond market. Opened by András Simor, Vice President and CFO, EBRD, it featured three panels and a number of keynote speakers including Alderman Alison Gowman representing the City of London's Green Finance Initiative, Stephanie J. Miller of the International Finance Corporation and Gert D. Wehinger, Senior Economist, OECD.

The first afternoon panel brought together GBP Executive Committee members who discussed the key innovations featuring in the GBP 2016 update followed by a Q&A. The second panel moderated by Peter Cripps of Environmental Finance addressed the key role in promoting market transparency played by exchanges, financial information and indices providers, as well as rating agencies with the participation of Nikhil Rathi, CEO, London Stock Exchange; Maurice Bauer, Secretary General, Luxembourg Stock Exchange; Laura Nishikawa, Executive Director, MSCI; Lenora Suki, Head of Sustainable Finance Product Strategy, Bloomberg; and Henry Shilling, Senior Vice President, Moody's.

The final panel moderated by Ulrik Ross of HSBC covered Green Bond perspectives in developing markets such as China and India, as well as the international policy dialogue on Green Finance taking place in particular at the G20. It included Jean Boissinot, Head of Banking and Financial Sector Analysis Division, Direction Générale du Trésor; Sean Kidney, Chief Executive, Climate Bonds Initiative; Namita Vikas, Chief Sustainability Officer, Yes Bank; Michael Bennett, Head of Derivatives and Structured Finance, World Bank Treasury; and Esohe Denise Odaro, Head of Bond Investor Relations, IFC.

Going forward the priorities of the GBP will be amongst others the implementation of the online GBP Resource Centre, the launch of the GBP 2016 consultation, the calibration of existing and/or new working groups with a focus on reaching out to GBP observers and stakeholders, and following up on developments related to the new *Guidance for Issuers of Social Bonds*.

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ESG factors at a critical intersection of sustainable development and fixed income investing

By Heike Reichelt and Christine Davies, World Bank, June 2016

A growing number of investors are integrating environmental, social and governance (ESG) factors into their investment decisions. While historically led by mission driven investors like faith-based organizations, universities, foundations and some pension funds, there is now a growing number of investors that are considering ESG factors using various approaches including:

- Negative or exclusionary screening → avoiding companies based on ethical, political or institutional considerations and/or principles.
- Best-in-class selection → asset selection based on ESG performance relative to sector peers.
- ESG integration → incorporation of ESG factors into the risk management and portfolio management processes.
- Active ownership → direct or proxy engagement and involvement with the investee company in order to address specific ESG issues.
- Impact investing → pursuit of specific and measurable beneficial social and/or environmental impacts alongside financial return. Generally, this approach can be implemented at a sector or thematic level.

Awareness and application of the various ESG approaches above into investment practice has varied across asset classes, with equities being the asset class where the most progress has been made thus far. However, incorporation of ESG into fixed income investment is increasingly the subject of both research and practice, particularly in the corporate sector. Given the size of the fixed income markets, the incorporation of ESG approaches into investment processes could have significant positive implications for directing capital to achieving sustainable global growth.

Four trends show potential to accelerate the integration of ESG factors into the fixed income investment decision making process.

First, there is a growing body of literature pointing to evidence that fixed income issuers with strong ESG factors outperform those that have weaknesses. Integration of ESG factors into equity investment decision making has increased significantly over the past five years, and several equity-related research studies have demonstrated that material ESG factors can contribute to excess returns over time.[17] However, there is now also research showing that these links may extend to fixed income markets as well. For example, according to a study by Barclays in November 2015, between 2007 and 2015 investment grade bonds with higher ESG scores outperformed those with low ESG scores, after controlling for systematic exposures such as sector, duration and quality. The study also found that high ESG scores generated a statistically significant return premium, with governance emerging as the strongest of the three.[18]

Second, there is increasing availability of ESG data published by organizations and

17. Zoltan Nagy, Altaf Kassam and Linda-Eling Lee, *Can ESG Add Alpha? An Analysis of ESG Tilt and Momentum Strategies*, MSCI ESG Research, June 2015; *The Socially Responsible Quant*, Deutsche Bank Markets Research, April 2013.

18. Linda-Eling Lee, Matt Moscardi, Laura Nishikawa and Ric Marshall, *2016 ESG Trends to Watch: Opportunities and Risk*, MSCI Issue brief, January 2016.

independent research firms and a number of efforts are underway to improve the quality and consistency of this data. For example, the Financial Stability Board (FSB) Task Force on climate-related disclosures is developing voluntary, consistent climate-related financial risk disclosures for use by companies in providing information to investors, lenders, insurers, and other stakeholders. The work and recommendations of the Task Force will help firms understand what financial markets want from disclosure in order to measure and respond to climate change risks, and encourage firms to align their disclosures with investors' needs. In April 2016, MSCI launched a sustainable impact index and metrics designed to allow institutional investors to measure their exposure to public companies whose products and services help to address major social and environmental challenges through a framework that aligns with the Global Goals for Sustainable Development. In March 2016, the World Bank and a group of multilateral development banks (MDBs) first published a harmonized framework for impact reporting for green bonds that has been welcomed by investors and led to a revised version supported by 11 International Finance Institutions (IFIs) in December 2016.

The third trend supporting ESG integration is driven by the increasing international consensus around the important role of the private sector in sustainable development. While just a few decades ago, many may have considered economic and social development to be the purview of the public sector, the three landmark multilateral agreements of 2015 – the Addis Ababa Action Agenda, the Global Goals for Sustainable Development, and the Paris climate change agreement – are evidence of the consensus that sustainable development cannot be achieved without vibrant participation of the private sector. These agreements do not rely solely on the public sector and MDBs; the private sector is viewed as a critical component to achieving the ambitious development agenda. These agreements represent an important transition to a new theory of change recognizing that the most enduring, sustainable, and scalable solutions to development problems have emerged through the interplay of private investment and public policy.[19]

- The Addis Ababa Action Agenda was an agreement for a new model for financing development that recognizes that development needs outstrip the fiscal capacity of the public sector and MDBs alone. Leveraging the private sector is essential.
- The 17 Global Goals for Sustainable Development set an ambitious agenda for development over the next 15 years. While each of the 17 goals is arguably essential for the private sector to flourish, "Goal 17: Revitalize the global partnership for sustainable development", explicitly references the urgent need to mobilize the transformative power of the private sector.
- The Paris Agreement on Climate Change signals a global commitment to address climate change -- an issue that will require trillions of dollars of capital to be spent in the coming decades curtailing greenhouse gas emissions and adapting to the effects of climate change that can no longer be avoided.

Not only will private sector investment be essential for achieving these ambitious international agreements, but astute investors will also factor in the probable regulatory changes that will be needed for countries to meet their commitments under these agreements to manage risk and seek opportunity in their portfolios.

*Fourth, more investors are considering environmental and social impacts in addition to financial factors in their investment decisions***.** According to a report by US SIF Foundation, more than one out of every six dollars under professional management in the United States were invested according to strategies of sustainable and responsible investing at the start of 2014: a 76% increase compared to just two years earlier.[20] The growth in signatories to the UN Principles for Responsible Investing (PRI) provides further evidence of this growth internationally. Launched in April 2006, the number of PRI signatories has grown from 100 to over 1,500 representing some US$62 billion in assets under management.

Furthermore, emerging instruments like green bonds, sustainable bonds, and social bonds make it easier for investors to add specific and measurable social and/or environmental benefits to their fixed income portfolios, while achieving the same level of risk-adjusted financial returns as traditional bonds issued by the same issuer. In 2008, the World Bank issued its first green bond. The bond was a plain vanilla SEK bond for mainstream investors and had a second opinion from CICERO evaluating its eligibility criteria and project selection process. Green bonds allow investors to direct funding towards projects that support the transition to a low carbon future. Since the World Bank's inaugural green bond, the market has grown significantly. Issuers have diversified beyond the multilateral development banks that pioneered the market to include local governments and agencies, utility companies and corporate issuers, and a growing number of investors are actively engaged in developing the market both announcing investment commitments and working with issuers to promote the credibility of the market and standardization, for example through the Green Bond Principles.

Social bonds or sustainability bonds are the logical progression from green bonds: they allow fixed income investors to support socially and environmentally sustainable priorities, of which green bonds are a subset specific to environment and climate change. The World Bank and other MDBs have been raising funds from investors for social purposes for decades and will play an important role in developing the growth of a broader social bonds market just as they did for green bonds.

19. Homi Kharas, *The Post-2015 Agenda and the Evolution of the World Bank Group,* The Brooking Institution, August 2015.

20. *US Sustainable, Responsible and Impact Investing Trends*, US SIF Foundation, 2014.

For example, at the World Bank all work is anchored in its twin goals to end extreme poverty and to promote shared prosperity in a sustainable manner, and the impact or results that the individual projects are expected to achieve and the actual delivery upon implementation is publically reported. Each World Bank project contributes to helping client countries meet the twin goals across the whole spectrum of sustainable development activities, spanning across health and social protection, education, food security, and critical infrastructure including water and sanitation, transport and energy. Furthermore, all World Bank projects are subject to the World Bank's environmental and social safeguard policies.

To support investors that are interested in a broader range of social and environmental impacts, the World Bank reports on the types of projects it finances, its project selection process, and the expected impact of the projects it supports. As an issuer of sustainable development bonds, the World Bank draws on its long and ample experience in rigorous project selection, measuring results and reporting on the impacts achieved by its funded projects in developing countries to make this information more easily available to investors.

In doing so, the World Bank contributes to the development of impact investment options for investors. The growth of the social bond market will also be supported by the *Guidance for Issuers of Social Bonds* recently published by the Green Bond Principles.

Green bonds, sustainable bonds, social bonds and emerging instruments offer fixed income investors the possibility to contribute to creating significant social and environmental benefits without compromising their financial objectives or changing their investment philosophies. This is an important innovation that is mainstreaming impact investing and putting it as an accessible option for different types of investors seeking high-quality assets.

For individual and institutional investors, putting their capital to work to affect positive social and environmental change is not just a responsibility, but more importantly it is an opportunity to extract gains and reduce risks from the global shifts that are taking place. In practice, for many investors developing robust and integrated approaches for assessing ESG factors in their investment portfolios – particularly fixed income portfolios – remains a work in progress. But the increasing availability and consistency of data, such as through new indices and frameworks for reporting ESG factors and social and environmental impacts, are important catalysts to accelerate this process.

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The opinions expressed here are the authors' and do not necessarily reflect those of the World Bank or its stakeholders.

International participation in China's domestic capital market

By Ricco Zhang

Introduction

After 20 years of existence, the Chinese onshore bond market has become the third largest bond market in the world. Since the International Monetary Fund's decision to include the Chinese currency in its Special Drawing Rights (SDR) currency basket in November 2015, Chinese policy makers have accelerated reforms to further open up the Chinese market to international participants, both issuers and investors.

Panda bonds

Panda bonds are fixed income securities issued by foreign institutions in China's domestic markets (both interbank and exchange). The first panda bonds were issued in 2005 by the International Finance Corporation (IFC) and the Asian Development Bank (ADB). Daimler AG was the first private corporation to issue panda bonds in 2014. Although they were the only three issuers in the first decade of the nascent panda bond market, in 2015 the issuance of panda bonds accelerated with new issuers entering the market, including sovereigns, financial institutions and corporates.

Approvals for panda bond issuance are currently granted case by case. However, draft panda bond rules are currently under development and are expected to be largely principle-based. ICMA has been working closely with key China authorities such as the People's Bank of China (PBOC) and National Association of Financial Market Institutional Investors (NAFMII) on the interbank market, as well as Shanghai Stock Exchange on the exchange-traded market, to help develop rules appropriate to the needs of both foreign issuers and domestic investors. ICMA has continued its joint working group with NAFMII under the UK-China Economic Financial Dialogue (EFD), under which ICMA and NAFMII plan to issue a study on panda bond regulations and issuance procedures from a foreign issuer's perspective. The report together with policy recommendations will be released concurrently with the 2016 EFD.

Foreign access to China's interbank bond market

In February 2016, during the G20 meeting of Central Bank Governors and Finance Ministers, the PBOC made the significant announcement that China's interbank bond market would be opening up to a wide array of foreign institutional investors. In May 2016, the PBOC and the State Administration for Foreign Exchange (SAFE) published implementation rules to give detailed guidance on documentation and operational requirements. This marks a major step toward market liberalization, as now a wide range of foreign institutional investors may access the Chinese domestic market without prior approvals, licences or quotas from Chinese regulators. Existing quota regimes such as Qualified Foreign Institutional Investor (QFII) and Renminbi QFII (RQFII) are less

> **A wide range of foreign institutional investors may access the Chinese domestic market without prior approvals, licences or quotas from Chinese regulators.**

relevant under the new rules and, if an investor chooses to access the interbank bond market in its capacity as QFII/RQFII, it will also need to comply with the new policy framework.

Foreign investors will have to comply with certain filing requirements, as well as onshore regulations that govern trading in the interbank market. In particular, each foreign investor must have an onshore bond account with China Central Depository & Clearing Co., Ltd. (CCDC) and/or Shanghai Clearing House (SHCH). Each foreign investor must also appoint an onshore settlement agent, which will in most cases be a Chinese bank.

Foreign investors are not yet allowed to trade in the domestic bond repo market. If and when the domestic repo market does open up to international participants, they may be required to use the China Interbank Market Bond Repurchase Master Agreement, which is largely based on the GMRA but adapted to the Chinese market.

Shanghai Free Trade Zone (FTZ) Bond Market

The China (Shanghai) Pilot Free Trade Zone (Shanghai FTZ), approved by the State Council of China to launch in 2013, is intended to facilitate currency exchange, RMB cross-border use and interest rate liberalization, among other things.

ICMA and SHCH jointly hosted an event in London in April to introduce the Shanghai FTZ bond market to international markets. In the pilot programme, the market is initially only open to offshore investors and is expected to be a mix of onshore issuances (CN ISINs) but with cash movements in offshore RMB (CNH). Through the Shanghai FTZ, international investors may use the Euroclear Bank-SHCH link as a single point of entry without any significant additional registration, filing or approval requirements; furthermore, market practice will be consistent with international practices. In particular, investors may participate through their existing accounts with Euroclear Bank to trade bonds directly without any extra burden. This will give all offshore investors convenience of operations, flexibility of investment plans and fewer concerns about cross-border fund transfer.

The first bonds to be issued through the Shanghai FTZ are expected this summer. The Chinese authorities have indicated that if this pilot programme is successful, the model of the Shanghai FTZ may be extended to the overall interbank bond market.

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Summary of practical initiatives by ICMA

There are a large number of practical initiatives on which ICMA is currently, or has recently been, engaged with, and on behalf of, members. These include:

Primary markets

1. *PSIF:* The Public Sector Issuer Forum (PSIF), which met in London on 20 June, discussed among other things a strategic plan drawn up in consultation with PSIF members.
2. *New issue processes:* The FCA's interim report on investment banking, which was published after Easter, focuses on IPOs. However, there are also questions for new issue processes in the debt market. ICMA responded to the FCA consultation on 25 May.
3. *Market Abuse Regulation:* ICMA has facilitated lead-manager consideration of pre-sounding and stabilisation under the Market Abuse Regulation, which came into effect on 3 July. The ICMA Primary Market Handbook's stabilisation materials are being updated.
4. *Prospectus Regulation:* ICMA has commented on the draft ECON report relating to the new EU Prospectus Regulation proposed by the European Commission with a view to ensuring that wholesale markets can function as efficiently as possible; and has continued to be in contact with the Presidency of the EU, relevant members of the European Parliament and a number of key national regulators to discuss members' concerns.
5. *Guarantor financial information in prospectuses:* ICMA has responded to a UK FCA consultation on guarantor financial information in prospectuses which are PD-compliant.
6. *Bank of Italy Article 129 rules:* ICMA has coordinated a joint letter to the Bank of Italy relating to the forthcoming Article 129 rules on post-issuance reporting.
7. *UK PRA Contractual Stay:* ICMA has met representatives of the UK Prudential Regulatory Authority (PRA) and the Bank of England to discuss the PRA's Contractual Stay rules, and has circulated standard language to address the rules in any relevant debt capital markets contracts.
8. *BRRD Article 55:* ICMA collaborated with AFME on updating a model clause to address contractual recognition of bail-in in relevant documentation. Jointly with the BBA, ICMA submitted a response to the UK PRA's consultation on the contractual recognition of bail-in.

Secondary markets

9. *Corporate Sector Purchase Programme:* ICMA has published a briefing note on *Further Thoughts on the ECB's Corporate Sector Purchase Programme,* following the ECB's announcement of details of the programme on 21 April. The ECB attended a meeting of ICMA's Secondary Market Practices Committee on 17 May.
10. *Electronic trading:* On 20 April, ICMA launched its study on the *Future of Electronic Trading*, prepared by Liz Callaghan. She also wrote an article on the subject for the Banque de France's *Financial Stability Review,* published in April.
11. *Corporate bond market liquidity:* On 6 July, ICMA published its *Second European Investment Grade Corporate Bond Secondary Market Study*, undertaken by Andy Hill, into the current state and evolution of the European investment grade corporate bond secondary market.
12. *Market Abuse Regulation:* ICMA has published a briefing note on the impact of the Market Abuse Regulation on Investment Recommendations.
13. *Review of ICMA buy-in rules:* Under the guidance of the Secondary Market Practices Committee, ICMA plans to consult members on possible revisions to ICMA buy-in rules so as to improve the efficiency and transparency of the buy-in process, while also supporting the possibility of a buy-in auction mechanism.
14. *Distributed Ledger Technology:* On 8 June, ICMA published on its website a resources page on Distributed Ledger Technology/Blockchain.

ICMA responses to consultations by regulators are available on the ICMA website.

Repo and collateral markets

15. *CSDR:* With members of the ICMA European Repo and Collateral Committee (ERCC), chaired by Godfried De Vidts, ICMA met officials from DG FISMA at the European Commission in Brussels on 15 April to discuss asymmetries in the operation of the proposed regime relating to settlement discipline under the Central Securities Depositories Regulation (CSDR).

16. *SFTR:* ICMA responded to the ESMA Discussion Paper on the EU Securities Financing Transaction Regulation (SFTR), with support from the ICMA ERCC Operations Group, on 22 April. In addition, ICMA, jointly with four other trade associations, published a statement which can be used to help market participants to comply with the new collateral re-use requirements under Article 15 of the SFTR.

17. *TARGET2-Securities:* The ICMA ERCC Operations Group submitted a response on 4 April to an ECB consultative report on the services provided to market participants as part of its Real-Time Gross Settlement System (RTGS). The consultation focuses on potential synergies between TARGET2 and TARGET2-Securities.

18. *Collateral re-use:* The ICMA ERCC submitted a response to the FSB's consultative proposals on *Possible Measures of Non-Cash Collateral Re-use.*

19. *NSFR:* To support its dialogue with officials, the ICMA ERCC has prepared a paper on the impact of the Net Stable Funding Requirement (NSFR) on repo and collateral markets. This paper has been used as the centrepiece of an ICMA ERCC response on 24 June to a related Commission consultation.

20. *Leverage Ratio:* The ICMA ERCC responded on 6 July to the BCBS' consultation on the Leverage Ratio, offering suggested recalibrations to refine the regime.

21. *Collateral optimisation:* The ICMA ERCC is providing input to help advance work on collateral being conducted under the auspices of the Commission's European Post-Trade Forum and, distinctly, the ECB's COGESI.

22. *European repo market survey:* ICMA is compiling European repo market survey data to provide a "snapshot" of repo business at close of business on Wednesday, 8 June 2016. This is the 31st such semi-annual survey.

23. *GMRA:* ICMA has published the 2016 legal opinions which support the use of the GMRA, the standard agreement used for international repo transactions, in over 65 jurisdictions worldwide.

Asset management and investors

24. *Fund liquidity:* On 18 April, ICMA's Asset Management and Investors Council (AMIC) launched, jointly with EFAMA, a report on *Fund Liquidity* in response to public concerns that liquidity is becoming more fragmented. The report sets out the legislative requirements and market-based tools available to manage liquidity risk in investment funds in Europe. Fund liquidity was one of the issues for discussion at the AMIC Council at the Banque de France on 4 April.

25. *Covered bonds:* On 23 May, the ICMA Covered Bond Investor Council responded to the *Review of the Covered Bond Label Harmonised Transparency Template: 2016*.

Capital market products

26. *Green Bonds:* The Green Bond Principles (GBP) held their second AGM in London on 16 June hosted by the European Bank for Reconstruction and Development. The GBP AGM was followed by the second annual GBP conference attended by nearly 300 participants. The key focus of both events was the 2016 update of the GBP.

Other meetings with central banks and regulators

27. *Bank of England:* ICMA was invited to two separate meetings with the Bank of England to discuss future cooperation: with Chris Salmon, Executive Director, Markets, on 12 May; and with Andrew Bailey, Deputy Governor, on 17 May.

28. *ESMA:* At its meeting in Paris on 16 June, the ICMA Regulatory Policy Committee had a discussion with Verena Ross, Executive Director, European Securities and Markets Authority.

29. *Official groups:* ICMA continues to be represented, through Martin Scheck, on the ECB Bond Market Contact Group; through René Karsenti, on the ESMA Securities and Markets Stakeholder Group; and through Godfried De Vidts on the ESMA Secondary Markets Standing Committee, the ECB Contact Group on Euro Securities Infrastructures (COGESI), the ECB Macroprudential Policies and Financial Stability Contact Group and the Bank of England's Securities Lending and Repo Committee (SLRC). ICMA is also an official member of China's Green Finance Committee under the auspices of the People's Bank of China, as well as the Green Finance Study Group under the G20.

Primary Markets

by Ruari Ewing and Charlotte Bellamy

EU prospectus regime

Prospectus Directive Review

As reported in previous editions of this Quarterly Report, ICMA is fully engaged with the current review of the European Prospectus Directive regime. The latest development is the agreement of a general approach by the Council of the European Union. This will form the basis of the Council's negotiating position in trilogue with the European Commission and Parliament.

The Council text makes a number of amendments to the draft Prospectus Regulation proposed by the European Commission on 30 November 2015. As ever, ICMA is focused on the impact of the proposed Prospectus Regulation on the cross-border vanilla bond market, and it is encouraging to see that some of the most concerning provisions in the Commission's text have been amended. So the proposals appear to be moving in a helpful direction generally, but there are some remaining concerns, particularly in relation to the new risk factor requirements. A summary of the key areas on which ICMA is focused is below.

(i) *Wholesale disclosure regime:* The Council appears to have reinstated the PD2 position with respect to the €100,000 minimum denomination threshold (ie there appears to be both a public offer exemption and differentiated disclosure for bonds with a minimum denomination of at least €100,000). It is very encouraging to see that the importance of having distinct wholesale and retail debt disclosure requirements has been recognised. Such a distinction is crucial in ensuring that Europe's wholesale bond market can continue to function efficiently and corporate borrowers can access the funding they need while providing an appropriate level of disclosure to the institutional investors to whom they offer securities. Differentiating between bonds with a minimum denomination of at least €100,000 or less than €100,000 per the current PD2 regime and the Council's general approach is indeed one way of achieving that, and has the benefit of being a clear regime that is easy to apply in practice. An alternative would be to provide an exemption from the prospectus summary requirement and a differentiated disclosure regime for prospectuses for admission to trading on a regulated market of bonds offered solely to qualified investors. That approach would have the benefit of encouraging issuers to issue in low denominations, which could in turn increase indirect retail access to debt securities. This will be important as Europe's population ages and retail investors are in ever greater need of capital markets investment opportunities. There are also a number of other, technical, advantages to a "qualified investor only" regime for issuers and institutional investors that ICMA has been discussing with regulators and MEPs. It is also worth noting that a "qualified investor only" approach was proposed by the then ECON rapporteur, Philippe de Backer, MEP in the draft ECON report (covered in the Second Quarter 2016 edition of this Quarterly Report).

(ii) *Risk factors:* The Council has amended the Commission's proposed requirement for issuers to categorise risk factors by materiality by suggesting that risk factors be categorised according to their type, with the most material risks being mentioned first in each category. The Council also envisages that the issuer *may* disclose its assessment of the probability of a risk materializing and the magnitude of the negative impact of such risk using a qualitative scale of low, medium or high. While this is likely to be seen as an improvement on the Commission text, there continue to be concerns that the provisions will raise liability questions for issuers. ICMA has communicated those concerns to certain national regulators and it is hoped that those points will be borne in mind as the legislative process progresses.

(iii) *Summaries:* The standalone requirement for the summary to be not misleading remains in the Council text, which is disappointing because it casts doubt on what appears to be the co-legislators' intention for liability to attach to the issuer only if the summary is misleading *when read with the rest of the prospectus*. In addition, the Council has retained a cap on the number of risk factors that can be included in the summary, albeit in a slightly different format to the Commission's proposal. This approach is also likely to raise liability concerns for issuers.

(iv) *20% limit for convertibles:* The Council appears to have tried to address concerns relating to the apparent need for a prospectus for securities issued as a result of recovery and resolution-driven actions under BRRD and the conversion of regulatory capital/loss absorbing capacity. These adjustments are helpful, although it is likely that the proposed language will require some technical amendments in order to fully address market participants' concerns in this area.

(v) *Third country issuer representative:* The Council has helpfully suggested that the new requirement for third country issuers to appoint a representative in the EU be amended to remove the liability element for the third country issuer representative.

(vi) *Implementation:* It is also very helpful that the Council has suggested that the majority of provisions would apply 24 months from the date of entry into force, rather than 12 months, as this should provide sufficient time for the necessary Level 2 requirements to be developed and finalised before the new regime applies in practice.

In terms of developments in the European Parliament, the original Economic and Monetary Affairs Committee (ECON) *rapporteur* (Philippe de Backer, MEP) stepped down in order to take a position in his national government, and was replaced by Petr Ježek, MEP. This change appears to have resulted in a slight delay to the expected timetable.

However various MEPs suggested additional amendments to the Prospectus Regulation in two separate documents (Amendments 135 to 347 and Amendments 348 to 649) following the publication of Philippe De Backer, MEP's draft ECON report in March 2016 (as reported in the Second Quarter 2016 edition of this Quarterly Report).

Many of the MEPs' proposed amendments appear to be helpful. However, there appear to be a number of concerning amendments removing debt issuers' flexibility to choose their home Member State for prospectus approval. This proposal has the potential to increase market fragmentation and, as such, would be a retrograde step away from the concept of a Capital Markets Union and a single internal market. Some justification given for the proposed changed is that the current regime could invite "regulatory arbitrage" or encourage a "race to the bottom", which is not the case. The Prospectus Directive is a maximum harmonisation Directive and the Prospectus Regulation will be directly applicable in all Member States. Regulatory arbitrage or a race to the bottom is therefore not possible. Corporate borrowers value the current flexibility afforded by the home Member State definition because it allows them to choose a national competent authority (NCA) with the expertise and resources to handle their debt transactions. Smaller markets' NCAs will be less well equipped to deal with complex debt transactions in a timely manner. Some evidence of this can be seen in a recent ESMA *Peer Review Report on Prospectus Approval Processes* (see further below). It is therefore hoped that these unhelpful suggested amendments are not taken forward by the European Parliament.

Once the European Parliament has finalised its position, the legislative process is expected to move to a stage known as trilogue, in which a final text is negotiated among the European Parliament, Council and Commission. We understand trilogue may begin in September 2016, as previously anticipated. This means that the new Prospectus Regulation could be published in the *Official Journal* at some point in the first half of 2017, and apply either 12 months or 24 months thereafter.

ICMA is continuing to engage fully with national regulators and official institutions and MEPs as the legislative process progresses.

Other developments under the current Prospectus Directive regime

As noted above, ESMA published a *Peer Review Report on Prospectus Approval Processes* on 30 June 2016. The peer review focused on the quality and consistency of the prospectus approval process of national competent authorities (NCAs). The peer review appears to conclude that staff involved in the prospectus approval function at NCAs have the requisite knowledge to meet the requirements of the PD regime, although there may be differing levels of efficiency at different NCAs. The peer review highlighted areas of the prospectus approval process that could be further harmonised, including approaches to risk factors. ESMA reports that recurrent concerns emerged as regards the comprehensibility of prospectuses (in particular base prospectuses) and that factors which could be seen as negatively impacting on comprehensibility included the overall length of the prospectus, the format of the summary, extensive risk factor and cover note disclosure, and the amount and manner in which information was incorporated by reference. Legislators are already seeking to address many of these themes in the proposed Prospectus Regulation.

ICMA also responded to two UK FCA consultations relating to the prospectus regime. First, ICMA submitted an informal email response on 9 May 2016 relating to proposed to Technical Note 604.2 on the PD advertisement regime, as envisaged in the UKLA Primary Market Bulletin No. 13, noting that the FCA may wish to consider whether and how any ESMA Q&A on the PD advertisement regime (which may be published in the coming months, as reported in the Second Quarter 2016 edition of this Quarterly Report) may affect the Technical Note. Second, ICMA submitted a response on 8 June 2016 relating to proposed Technical Note 634.1 on financial information on guarantors in debt prospectuses and requests for omission, as envisaged in the UKLA's Primary Market Bulletin No. 14, welcoming the Technical Note and highlighting some minor areas that the UKLA may wish to consider clarifying.

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Bank recovery and resolution

Contractual recognition of bail-in

Model clause update: ICMA has worked with AFME to update the model clause for contractual recognition of bail-in pursuant to BRRD Article 55 of "other liabilities" (ie not debt securities but liabilities arising under other third country law governed contractual documentation) that was previously mentioned on page 45 of the First Quarter 2016 edition of this Quarterly Report. The updated clause was prepared following the adoption by the European Commission of a Delegated Regulation with regard to certain BRRD-related regulatory technical standards. While there were some small differences between the provisions adopted by the European Commission and the final EBA RTS on which the original model clause was based, those differences were not felt to necessitate a change to the model clause. Rather, the changes to the model clause reflected comments received from market participants and market practice developments in the intervening period following the finalisation of the original model clause.

UK Prudential Regulation Authority Supervisory Statement on Contractual Recognition of Bail-in: The UK Prudential Regulation Authority (PRA) published Policy Statement PS17/16 and Supervisory Statement SS7/16 on 29 June 2016, following a consultation on amendments to the PRA rules relating to the contractual recognition of bail-in to which ICMA submitted a joint response with the BBA on 16 May 2016.

The key area of focus for ICMA's primary market constituency was the PRA's proposed guidance in relation to the "impracticability" exclusion from the requirement to include a contractual recognition of bail-in in non-EU law governed contracts, which is included in the Supervisory Statement. The Supervisory Statement is unchanged from the version originally proposed by the PRA, and the PRA notes that it expects BRRD firms to make their own reasoned assessment with regard to impracticability.

Contractual Stays

As reported in the Second Quarter 2016 edition of this Quarterly Report, the PRA rules in relation to contractual stays in financial contracts governed by third-country law prohibit in-scope firms from creating new obligations or materially amending existing obligations under certain non-EEA law governed financial arrangements unless the counterparty has agreed to be subject to similar restrictions on termination to those that would apply as a result of a UK firm's entry into resolution or the application of crisis prevention measures if the financial arrangement were governed by the laws of any part of the UK.

The rules are now in force in respect of third-country law financial arrangements with counterparties which are credit institutions or investment firms and, despite some uncertainty in relation to the precise scope of the rules, market practice in primary debt capital markets appears to be moving towards a settled position. ICMA worked with a number of law firms and through its Legal & Documentation Committee to develop a suggested clause for firms to use in relevant primary debt capital markets documentation. That clause has been circulated to the relevant ICMA primary market committees and working groups and is available from ICMA staff on request.

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> The extent to which market soundings and stabilisation will continue to be effective tools to mitigate market volatility remains to be seen.

Market Abuse Regulation: primary markets

Further to the Second Quarter 2016 edition of this Quarterly Report, the new Market Abuse Regulation (MAR) regime came into force on 3 July, with various Level 2 measures being finalised and published only recently around the soundings and stabilisation topics that ICMA has been focusing on in the primary markets context:

- Delegated Regulation EU/2016/960 on sounding procedures published on 17 June;
- Implementing Regulation EU/2016/959 on sounding templates published on 17 June;
- Delegated Regulation EU/2016/1052 on buy-backs and stabilisation published on 30 June; and
- Implementing Regulation EU/2016/1055 on public disclosure of inside information (relevant also to public disclosure of stabilisation) published on 30 June.

ESMA also published responses to its January consultation *inter alia* on buy-side sounding guidelines.

ICMA's most recent committee and working group deliberations have mainly focused on the implications of the rules for sounding information other than inside information, especially in relation to investor meetings (where a transaction might subsequently follow) and MTN (and SSA) price levels – with considerations notably on what constitutes transaction announcement, acting on issuer behalf and gauging interest (in contrast to negotiating terms). ICMA also organised a workshop for investors in Stockholm on 22 June (with publicly available slides on MAR generally, on insider lists, managers' transactions and investment recommendations and on soundings, stabilisation and STORs). ICMA is also updating Chapter 9 and Appendix 15 on stabilisation of the ICMA Primary Market Handbook, with publication targeted over the summer. There have also been some regulatory discussions on investment recommendations, including in the new issues context, which are covered in the secondary markets section of this Quarterly Report.

It may well take some time (months, if not more) for market practitioners to become comfortable with the implications of all ramifications of the new regime. The extent to which market soundings and stabilisation will continue to be effective tools to mitigate market volatility (particularly in the context of a future bear market) remains to be seen.

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Packaged retail and insurance-based investment products (PRIIPs)

Further to the Level 2 ESAs' consultation (reported in the First Quarter 2016 edition of this Quarterly Report) and the response (and related letters) of the Joint Associations Committee (JAC) on Retail Structured Products (reported in the Second Quarter 2016 edition of this Quarterly Report), the ESAs adopted final draft regulatory technical standards on 31 March (and published them on 7 April), with European Commission adoption of a consequential Delegated Regulation following on 30 June. The PRIIPs regime is due to enter into effect from January 2017.

The European Commission also responded to one of the JAC's related letters, including noting that the PRIIPs' regime territorial scope does not extend to offers by an EU manufacturer via a non-EU intermediary to a non-EU retail investor.

ICMA's focus, other than supporting the JAC, continues to be on ensuring the vanilla funding markets are not adversely impacted by the PRIIPs regime's ambiguous scope and incoherent substantive provisions. In this respect, it seems there is emerging market consensus that straight fixed rate and floating rate notes are out of PRIIPs scope – with ongoing focus on whether additional product features may have an impact from a product scope perspective. ICMA is also intending to foster in the early autumn (ahead of late 2016 debt programme updates/supplements) practical means of otherwise remaining out of PRIIPs scope – namely in terms of avoiding MiFID retail investors (such as updated selling restrictions, document legends and possible additional order book diligences).

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ECP market

ABCP: As reported in Issue 39 of the ICMA Quarterly Report, on 30 September 2015, the European Commission published details of its securitisation initiative; and as reported in Issue 40 of the ICMA Quarterly Report, in December 2015, the European Council reached agreement regarding its negotiating stance on this Commission proposal. Meanwhile the European Parliament has been working to develop its position, led on the STS file by its *rapporteur*, Paul Tang, MEP; and on the associated CRR revision file by its *rapporteur* Pablo Zalba, MEP. On 6 June 2016, these *rapporteurs* respectively published a draft STS report and a draft CRR revision report, both of which include concerning elements.

Critical commentary on the draft STS report has particularly noted the proposed 20% risk retention requirement. But of more specific interest from an ABCP standpoint is the proposal that "transactions within an ABCP programme shall be backed by a pool of underlying exposures that are homogeneous in terms of asset type and shall have a remaining weighted average life of no more than one year and none shall have a residual maturity of longer than three years." This compares with the Commission's version of this language in which the remaining weighted average life should be of no more than two years. Yet overall both these versions compare unfavourably to the Council's agreed position that "the pool of underlying exposures shall have a remaining weighted average life of not more than one year and none of the underlying exposures shall have a residual maturity of longer than three years, except for pools of auto loans, auto leases and equipment lease transactions which shall have a remaining exposure weighted average life of not more than three and a half years and none of the underlying exposures shall have a residual maturity of longer than six years."

Amongst concerns linked to the draft CRR revision report, of specific note for ABCP is a proposal to simplify the hierarchy of approaches by disallowing, for STS securitisations, the use of the securitisation external ratings-based approach (ERBA) in all cases. This is contradictory to both the Commission's proposal and the Council's agreed position; and, were it to be adopted in the final legislative text, is expected to cause particular difficulties for firms utilising the internal assessment approach, derived from ERBA, in relation to multi-seller ABCP conduits.

On 27 April 2016, ESMA provided an update on reporting information on structured finance instruments (SFIs) under the CRA Regulation (CRAR). The CRAR requires issuers, originators and sponsor entities to report information in respect of SFIs to ESMA. ESMA is responsible under CRAR for setting up a website where information on SFIs should be published (the SFI-website). The European Commission's associated Delegated Regulation requires that "the reporting entities shall submit data files in accordance with the reporting system of the SFIs website and the technical instructions to be provided by ESMA on its website". ESMA was required to issue these technical instructions by 1 July 2016, as the reporting obligations will apply from 1 January 2017.

ESMA has encountered several issues in preparing the set-up of the SFI website, including the absence of a legal basis for the funding of the website. Consequently, it is unlikely that the SFI website will be available to reporting entities by 1 January 2017. Similarly, ESMA was not in a position to publish the technical instructions by 1 July 2016. Given these issues, ESMA does not expect to be in a position to receive the information related to SFIs from reporting entities from 1 January 2017. This puts issuers, originators and sponsors in the potentially awkward position of being subject to disclosure obligations that are impossible to comply with. It might well be that the EU's STS Regulation will be used to officially address this concern, but the delay in the progress of this legislative proposal could mean it will not now come into force soon enough. In this case other official steps to resolve the concern may be forthcoming, but in practical terms the absence of the SFI website seemingly obviates the need to report.

MMFs: On 15 June 2016, the Permanent Representatives Committee (COREPER) agreed, on behalf of the European Council, a negotiating stance on the Commission's proposed EU MMFR; and the Commission welcomed this agreement. The Council confirmed COREPER's agreement at a meeting on 17 June 2016, and asked the Presidency to start talks with the European Parliament. The Parliament's ECON Committee already approved its negotiating stance back in March 2015. Since there are quite some differences amongst the original Commission proposal, the Parliament's version and this latest Council version, it remains to be seen what final provisions will be included in the MMFR once an agreed version is negotiated amongst these three proponents; and it remains unclear how long it will be before such an agreement can be reached.

Reacting to the adoption of the Council's position, on 20 June 2016, IMMFA welcomed the Council's pragmatism in permitting fund ratings to be sought by MMF managers, and in providing for an implementation period that allows investors, managers and service providers to ready

According to Article 8 of the Council's version of the MMFR, "eligible assets" for MMFs include eligible securitisations and ABCPs.

themselves. Nevertheless, IMMFA is disappointed that the restriction of government debt as a liquid asset means that government debt stable NAV funds and the low volatility NAV funds may ultimately prove unworkable. IMMFA believes that, if properly constructed, these structures would provide security and optionality for investors.

According to Article 8 of the Council's version of the MMFR, "eligible assets" for MMFs include eligible securitisations and ABCPs. Article 10 then details what are eligible securitisations and ABCPs. These must be sufficiently liquid and of high quality pursuant to the MMF's internal credit assessment according to rules laid down in the MMFR; and (i) qualify as a level 2B securitisation in accordance with Article 13 of the EU Delegated Regulation for the LCR, or (ii) be an ABCP issued by an ABCP programme which is fully supported by an EU credit institution supervised under the CRD and not have underlying exposures which are themselves securitisations, or (iii) be identified as a simple, transparent and standardised (STS) securitisation or ABCP, in accordance with regulations to be put in place.

In addition, short term MMFs, as defined in the MMFR, may generally only invest in such securitisations and ABCP assets where they have a residual maturity or legal maturity at issuance of 397 days or less; whilst for standard MMFs, as also defined in the MMFR, the limit is for a residual maturity or legal maturity at issuance of less than or equal to two years, provided that the time remaining until the next interest rate reset date is less than or equal to 397 days. Furthermore, Article 14 specifies that the aggregate of all exposures to securitisations, including ABCPs, shall be limited to either (i) 20% of the assets of a MMF, or (ii) 25% of the assets of a MMF, if the MMF invests at least 10% of its assets in securitisations or ABCPs identified as STS.

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Reform of the French CP Market

The French authorities have adopted a reform (French language version) to the legal framework of their commercial paper and medium-term note market.

This reform aims to open the market up to a larger number of issuers from France and other countries, as well as broadening its investor base. The market could also be opened up to mid-sized enterprises, which account for a major share of growth and jobs and are bound to make greater use of market financing. In keeping with the CMU project launched last year by the European Commission, the reform aims to improve allocation of resources and ensure greater diversification of financing. It provides new classes of assets, creating solutions for both investors and borrowers through access to broader bases of investors and issuers across different countries. It also meets the needs of economic players without jeopardising the market's transparency, accessibility or competitiveness. Amounts outstanding on the market are bound to vary according to the players' needs and business cycles.

The reform is enacted by Decree n° 2016-707 of 05/30/2016 and an Order of 05/30/2016 issued subsequent to the opinion of the European Central Bank of 30 March 2016. While the reform does not change the legal nature of the debt instruments, market functioning and supervision, or collateral eligibility rules for Eurosystem refinancing, it does merge negotiable debt paper with maturities of up to one year into a new category called "*titres négociables à court terme*"; with this paper having the new trade name of *"Negotiable European Commercial Paper"* (NEU CP, pronounced "new CP") chosen by the marketplace.

Amongst other things the reform also makes it possible to draft the information memorandum in a language commonly used in financial matters, other than French, with no requirement to provide a summary in French; and opens the market up to more international issuers with broader acceptance of the local accounting standards of countries in the EEA, and of accounting and auditing standards that the Commission recognises as equivalent to European standards in the case of third-country issuers. Efficient post-market infrastructures are provided that enable dealers to request ISIN codes (new *eNEU CP* tool) that are then generated in real time. This system, backed up by settlement in central-bank money, is intended to enhance the efficiency and legal certainty of transactions.

A transitional period will give issuers the time they need for the annual update of their financial information memoranda. Further information can be found on the Banque de France website.

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Other primary market developments

Italy Article 129 reporting requirements: ICMA, together with several other trade associations, supported a letter to the Bank of Italy prepared by Allen & Overy LLP regarding the forthcoming post-transaction reporting rules that, broadly speaking, will apply to certain debt securities offered to Italian investors or issued by Italian issuers from 1 October 2016. It is hoped that the Bank of Italy will consider the requests made by market participants in advance of the rules coming into force.

Updated FATCA language: With the help of a number of law firms and the ICMA Legal & Documentation Committee, ICMA's suggested FATCA language for vanilla debt programmes of non-US issuers has been updated. The changes to the suggested disclosure language were driven largely by the remoteness of the FATCA withholding risk on payments under securities issued under non-US issuers' vanilla debt programmes in light of, among other things, the prevalence of intergovernmental agreements between the US and a number of jurisdictions to implement FATCA. The updated language has been circulated to the relevant ICMA primary market committees and working groups and is available from ICMA staff on request.

Benchmarks: As reported in previous editions of this Quarterly Report, ICMA has been engaging with the process for the evolution of LIBOR and EURIBOR. In particular, ICMA has been focusing on contractual continuity of the terms of outstanding vanilla floating rate notes that reference those benchmarks and the need to eliminate or reduce the risk for confusion in the evolution of benchmarks, which could lead to market disruption and potentially litigation. In this regard, ICMA is considering carefully an EMMI Roadmap for the evolution of EURIBOR that was published recently. Helpfully, there seems to be a consensus emerging that the ICE proposals in relation to the evolution of LIBOR (see this ICE LIBOR Roadmap for the evolution of LIBOR) may not result in fallbacks being triggered under typical vanilla bond terms and conditions that reference LIBOR.

FCA Investment and corporate banking market study: On 25 May 2016, ICMA responded to the UK FCA's *Investment and Corporate Banking Market Study Interim Report* (and related Occasional Paper No. 15 on IPO allocations). The response noted the FCA's analysis work on alleged IPO allocation skews was incomplete and looked forward to the FCA's completed analysis in this respect. The response also noted the difficulty in specifically responding to the FCA's alleged read-across into debt, since no rationale for the FCA read-across was given, debt markets differ generally from equity and substantial debt data has already been delivered to the FCA in this respect but not been commented on in the interim report.

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Secondary Markets

by Andy Hill and Elizabeth Callaghan

ECB's Corporate Sector Purchase Programme (CSPP)

Technical parameters of the CSPP

On 21 April 2016, ICMA published a briefing note discussing a number of considerations related to the potential implications of the ECB's Corporate Sector Purchase Programme (CSPP) for European corporate bond market liquidity and investor and issuer behaviour. The note also identified the key components of the Programme that would ultimately determine its market impact, including bond eligibility for purchases, the allocation of purchases across countries and issuers, the split between primary market and secondary market purchases, and, most importantly of all, the intended size of CSPP purchases.

On the same day, following the meeting of the Governing Council, the ECB published further details of the CSPP, answering some of these questions. On 2 June 2016, the ECB published a Q&A on the Programme.

The technical parameters of the CSPP outlined by the ECB are as follows:

- The CSPP will be conducted by six Eurosystem central banks: Belgium, Germany, Spain, France, Italy, and Finland.
- Purchases will be made in the primary and secondary markets.
- Eligible bonds will have a minimum IG credit rating from at least one of the four main rating agents.
- Eligible bonds will have a remaining maturity of greater than six months and shorter than 30 years.
- Eligible issuers will be incorporated in the euro area. Issuers incorporated in the euro area whose ultimate parent is not based in the euro area will also be eligible, so long as the issuer is not a credit institution or an asset management vehicle.
- Purchases of individual ISINs will be limited to 70% of the outstanding issue size.
- A "benchmark" will be determined based on the market capitalization weighting of issuance across jurisdictions to help ensure proportionality and a diverse portfolio of purchases.
- CSPP holdings will be made available for repo and securities lending by the relevant NCBs.

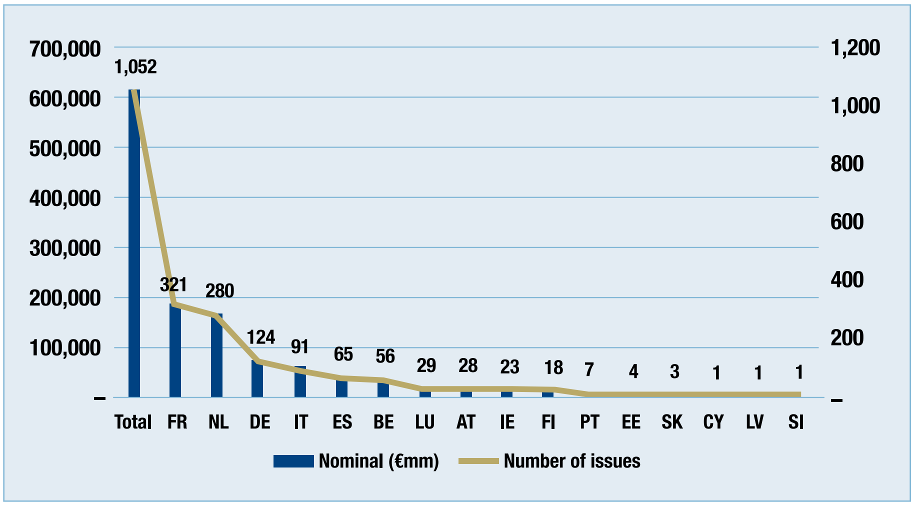
Universe of eligible bonds

As discussed in our earlier note, the key determinant in estimating market impact will be the size of purchases relative to the universe of eligible bonds. The details provided by the ECB help in estimating the latter. It would appear that the ECB is trying to keep the pool of potential purchases as deep as possible (including all remaining maturities from six months to 30 years, as well as issuers parented outside of the euro area). According to metrics available on Bloomberg, this would bring into scope 1,052 outstanding secondary market issues with a total nominal value of €617 billion.

Given relatively poor liquidity conditions in the European corporate bond secondary market, we continue to take the view that secondary market purchases will be relatively limited and opportunistic, with a skew towards purchases in the primary market.

The charts oppostie show the estimated distribution of eligible secondary market issuance across the various Member States. Interestingly, and quite importantly, the ECB intends to weight its purchases based on such a distribution, rather than applying the capital key used for sovereign purchases, or based on where it considers that it is likely to have the most impact in terms of supporting local credit markets.

Estimated secondary market universe of eligible bonds for CSPP purchases



COUNTRY	TOTAL	FR	NL	DE	IT	ES	BE	LU	AT	IE	FI	PT	EE	SK	CY	LV	SI
ISSUES	1,052	321	280	124	91	65	56	29	28	23	18	7	4	3	1	1	1
NOMINAL (€MM)	617,531	190,224	170,036	72,851	65,702	40,028	33,025	15,695	10,433	9,653	5,203	2,027	983	1,130	200	75	265
AVERAGE ISSUE SIZE (€MM)	587	593	607	588	722	616	590	541	373	420	289	290	246	377	200	75	265

Data source: Bloomberg

Lending facilities

Another important determinant for market impact is the availability of purchases into the repo and securities lending markets. As with purchases made under other components of the Asset Purchase Programme (APP), purchased securities will be made available, on a cash neutral basis, via the holding national central banks. This could lead to potential dislocations in the repo market since each national central bank has its own unique lending facility or mechanism, with different terms and arrangements. For instance, to borrow bonds from the National Bank of Belgium, counterparties will need to have in place a repo contract with the NBB. Meanwhile, the Bundesbank makes APP purchases available through Clearstream's automated securities lending service, while the Bank of Spain utilizes both bilateral repo agreements and Euroclear's automated lending programme. Furthermore, all of these different mechanisms have varying terms, costs, haircut criteria and collateral eligibility.

There have been growing calls for the ECB to create a centralized and harmonized lending facility for its sovereign purchases; but the argument for a central and easily accessible facility for corporate bond purchases could be even more compelling, particularly given an upper limit on individual purchases of 70% of outstanding issue size. Without the comfort of a liquid and accessible repo market, dealers are unlikely to risk taking a short position in any eligible bond, which, in turn, has important implications for secondary market liquidity.

ICMA's interaction with the ECB

In May, ahead of the start of the CSPP, the ECB attended the meeting of the ICMA IG Corporate Bond Secondary Market Practices Committee (SMPC) to discuss the Programme. This allowed ICMA's sell and buy-side members active in the European corporate bond market the opportunity to share their concerns with the ECB, as well as to provide constructive recommendations. ICMA, through the SMPC, intends to remain in close contact with the ECB as the Programme advances, and to act as a sounding board for the impact of the CSPP as it affects the functioning and liquidity of the European corporate bond market.

Purchases under the CSPP commenced on 8 June 2016. According to the ECB website, as of 1 July 2016, total CSPP holdings stood at €6,798 million.

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The evolving landscape of cash bond electronic trading in Europe

Background

Traditionally, fixed income markets have been a combination of voice market-making and intermediation (using inter-dealer brokers and hybrid voice-electronic systems to source liquidity), organised largely around banks (broker-dealers) and a relationship-based network of clients. The model has primarily been:

- broker-dealer to client: bank to asset manager, insurance company, or pension fund manager (the "buy side");
- broker-dealer to dealer: bank to bank or bank to inter-dealer broker (IDB);
- but not client to client: asset manager to asset manager.

The market practice has typically been based on market-makers, which are mostly broker-dealers which provide two-way pricing to their clients in a range of bonds, regardless of their ability to find an opposite seller or buyer at the same time, not least since the simultaneous "coincidence of want" can be highly improbable in bond markets. Where clients are sellers of a bond, the market-maker will show a "bid" and take the bond onto its own book, which it then hedges and looks to sell, either to another client or another broker-dealer, at a later time. Where clients are buyers of a bond, the market-maker will show an "offer" and sell the bond, which it will cover via the repo market. If it leads to a short-sell, the market-maker will hedge and look to buy back in the market at a later time.

Furthermore, a successful broker-dealer requires three interdependent components in order to offer viable market-making to counterparties:

- ability to hold inventory on balance sheet;
- a liquid repo market in order to fund long positions or cover short sales;
- the capacity to hedge in the derivatives markets.

These three components have become more challenging, due to prudential capital adequacy and leverage rules causing balance sheets and derivatives markets to become far more expensive. As regulatory pressures reduce the capacity for broker-dealers to hold, finance or hedge trading positions, the traditional source of bond market liquidity is being eroded. It is important to note that the market structure in fixed income for dealer-to-client has always been identified as "quote-driven" (versus the more electronic "order-driven" in equities). Prices are only offered in response to a counterparty request for quote (RFQ). Because this is unidirectional, details of price formation (including actual volume and size) are not shared with the public. Therefore, quotes and trade prices for an individual bond can contrast widely depending on the broker-dealer.

Drivers for change: An electronic trading tale of two asset classes

Like equities fixed income trading will have its successes and failures. But will cash bond electronic trading in Europe evolve the same as equities? The short answer is no. However, there will be some similarities. Let us look at the story of equities electronic trading in Europe and compare it to what is happening in the cash bond European electronic trading space.

Equities story: why did the equities model change?

In equities, the buy side wanted to increase efficiency, reduce trade failures and gain more control over their execution. This then led them to look at efficiencies in how they executed. The buy-side started to investigate if the manner of execution could become more efficient. Buy side blotters in equities in the early days generally had an 80/20% liquid/illiquid split. This meant 80% of the orders (order-driven market) were easy to trade and available (which is defined as "liquid") and the 20% were large or tricky to trade and needed sell-side assistance and balance sheet or "risk" as it was usually referred to. So the market began to see new efficient initiatives such as Direct Market Access (DMA) and algorithms ("algos" complex computer programmes following a defined set of instructions) to route the 80% easy-to-trade orders via broker networks straight to exchanges or agency only execution platforms. Direct Market Access and algos allowed clients directly to access execution venues, using the broker-dealer's membership as well as their "pipes and plumbing".

- *Early equities*: Phone-driven with on-screen IOIs (Indications of Interest) but no real-time electronic execution. Combination of agency, proprietary and principal trading. Open to abuse as brokers did not have to stand by their IOIs ("phishing" quite prevalent) and priorities between proprietary trades and client trades often became blurred.
- *Evolved electronic equities trading:* Proprietary trading is restricted (due to regulations such as the Volcker rule affecting American firms), principal trading has diminished as equities have become liquid enough to create order book electronic markets and therefore the demand for risk has more or less disappeared; technologically savvy execution with an audit trail; much more (firmer and realistic) pre-trade and post-trade information available to market participants.

Bond story: is fixed income trading ready for change?

Yes, and no. Technology is advancing automation in fixed income trading but fixed income markets are significantly different to equities. The fixed income evolutionary path will be different to equities. The equities market is more about "electronic" trading with characteristics of speed and artificial intelligence (algorithmic and high frequency trading). Whereas fixed income trading is more about "automation", with desired characteristics of efficiency, optimisation and – particularly – sourcing. It is important to note the similarities and differences in the evolution of both bonds and equities electronic trading. With this data, firms will be better able to gauge the direction of travel for bond electronic trading in Europe and make informed decisions.

Fixed income and equities similarities:

- *Technology:* Order Management Systems/Execution Management Systems, FIX Protocol, phone driven with on-screen IOIs (Indications of Interest).
- *Buy-side control:* informed decisions with buy-side having more input to price formation. Performance measurement on every stage of the trade including pre and post. Understanding of how execution contributes to fund performance.
- *Regulations:* causing a fundamental shift in market structure. Creation of transparency based rules and ideally, increased orderly functioning of the market.

Fixed income and equities divergence:

Equities:

- Equity Instruments: 6,810 shares admitted to trading on regulated markets in the EU trade 400 times per day on average.
- Commission-based.
- Order-driven with Straight Through Processing (STP), using FIX protocol enabling full end-to-end trading with audit trail.
- DMA to exchanges using bank's pipes and plumbing.
- Heavy use of algorithmic trading for electronic statistical and rules based trading in an agency environment.

Bonds:

- Over 150,000 debt securities (contained in Xtrakter's Computer Updated International Database [CUPID]) on average trade 1.5 times per day[21].
- Quote-driven relying on RFQs.
- Different characteristics: each bond can have a different maturity, coupon and rating.

21. Biais and Declercq: Academic Study, 2007 and ICMA published article, 2009.

- Heavy use of OTC markets with market-making and balance sheet usage.
- Heavy use of IDBs.

Flexible (and increasingly electronic) strategies for bond trading

In the case of equities, execution strategy drove the development and style of electronic trading. In fixed income the perception of percentage split of liquid versus illiquid cash bonds is quite the opposite. There are many more illiquid bonds than illiquid equities. These illiquid trades need strategies that will have the least amount of information leakage and market impact possible. The combination or market impact and information leakage negatively impacts price formation in bond markets and also damages best possible result for the underlying client. The impact is felt more as there is much more illiquidity in bond markets. So for the least amount of market impact, a fixed income buy-side trader will split his orders into categories, split between time sensitive (where immediacy is key), non-time sensitive, illiquid and liquid.

- *Time sensitive – illiquid:* requires strategies or protocols that involve some form of bilateral negotiation such as voice OTC, OTC market-making or RFQs. There is a sense of immediacy and due to illiquidity, possible market impact.
- *Time sensitive – liquid:* requires multilateral low-touch protocols such as all to all, continuous auction with no worry about market impact as information leakage is not important.
- *Non-time sensitive – illiquid:* requires protocols that are a combination of multilateral and bilateral, with an anonymous twist. The order can sit and wait for the other side or at the very least the best price. The order interacts anonymously with other participants but there is a negotiation phase before execution. There is no market impact as there is zero chance of information leakage.
- *Non-time sensitive – liquid:* requires trading multilateral protocols that are low-touch, such as Central Limit Order Books (CLOBs) or Smart Order Routing (SOR) technology to multiple CLOBs. The key element to point out when comparing and contrasting equities to fixed income is that equities are about electronic trading (speed) whereas fixed income is more about the "automation" of trading (optimisation).

For trading desks, the priority will be achieving the flexibility necessary to access bond liquidity across multiple counterparties and trading platforms while using a variety of protocols. The stage is set for a business model that has more in common with equities electronic trading than ever before.

Reshaping business strategies

In order to endure, bond trading must adapt and innovate. This will involve all facets of trading including people, a re-direction of business strategy and increasingly, technology. So, what are market participants doing? The smart ones are adapting and optimising the business and strategies they currently have and are investigating profitable opportunities for the future. They are modifying portfolio construction based on expected liquidity, reviewing broker coverage and service levels and revising regulatory impacts on trading.

Today, broker-dealers are identifying priority clients and assessing the clients by opportunities to cross-sell rather than single-product (or region) sales strategies. For example, clients need to be a "client" for more than one business line such as derivatives, emerging markets, equities or possibly even a revenue producer in other global regions. Hence for many, the old market-making model is disappearing.

This is having a knock-on effect. Banks are restructuring and redirecting their strategies. They are becoming agency brokers focused on electronic execution, niche players or getting out of certain areas of the bond business altogether. Some wonder if the traditional notion of capital commitment through monetising the bid-ask spread is becoming a less appropriate method of bond trading, suggesting the market could move to a more commission based electronic model. With a commission-based model, overheads relating to regulatory change (eg IT costs) might be passed on to clients more easily through commission rates (which are more standardised).

Buy sides as well as sell sides are restructuring and redirecting their business strategies. The costs involved in meeting regulatory requirements are escalating dramatically. The industry's view is that, when MiFID II comes into effect, there may be an increased risk that some buy sides may end up deselected as clients by broker-dealers, whilst many smaller sell sides will not have the resources to build IT facilities required by the law and will therefore have to electronically outsource their trading activity to larger houses.

Conclusion

While some of the above may sound like doom and gloom. This is not the case at all. "Change brings opportunity." A good example is small niche brokers. Niche brokers are smaller sell-side dealers consolidating their businesses, relying on a leaner model of reduced trading and sales teams but increasing the use of electronic trading platforms in order to reach more investors. These participants are realising the opportunity to becoming the new specialists in certain sectors or segments within the bond markets, particularly credit. They are achieving this through combining *electronic trading and sourcing with a directed balance sheet*. This type of innovative opportunism is set to continue.

As we saw with equities, outmoded trading models were cast off to make way for new electronic ones. Opportunities emerged. In bond trading this is happening today and will continue in the near future and beyond. Old ways are dying out but new ways of trading are emerging. They are innovative and use technology based solutions to face business and market challenges. These new "traditions" are set to be with us for the next 5 to 10 years and beyond.

More on the evolution of electronic trading in bonds can be found on ICMA's website.

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Market Abuse Regulation: Investment Recommendations

Background

Under the Market Abuse Regulation (MAR), an Investment Recommendation is defined as: "information recommending or suggesting an investment strategy, explicitly or implicitly, concerning one or several financial instruments or the issuers, including any opinion as to the present or future value or price of such instruments, intended for distribution channels or for the public".

There have been changes from the previous Market Abuse Directive (2003): most importantly, the removal of Recital 3. This is why the industry is focusing so heavily on the Market Abuse Regulation's Investment Recommendations.

Previously under Market Abuse Directive (2003), Recital (3)*:* "investment advice, through the provision of a personal recommendation to a client in respect of one or more transactions relating to financial instruments (in particular informal short-term investment recommendations originating from inside the sales or trading departments of an investment firm or a credit institution expressed to their clients), which are not likely to become publicly available, should not be considered in themselves as recommendations within the meaning of this Directive".

Recital 3 no longer exists under MAR:

(i) Market Abuse Regulation: Investment Recommendations

The FCA has stated that it will take a "pragmatic proportional approach" to the MAR Investment Recommendations and how communications are categorised.

The FCA considers there are only two types of regulated recommendations, either an *Investment Recommendation* or a *Personal Recommendation.*

- There are certain communications that are neither, such as recommendations that relate to instruments that are not in scope of MAR, recommendations that relate to a sector rather an instrument, and communications that convey a purely factual message or simply do not contain a recommendation.
- It is up to firms to determine whether a communication is an Investment Recommendation under MAR, a personal recommendation under MiFID II, or neither.
- The buy side will apply judgement on a case-by-case basis, in the same way as the sell side.

(ii) MAR Investment Recommendations: Rules

Any Investment Recommendation made to a client must be accompanied by the appropriate disclosures. For further information, please click here. Our understanding of what is in scope and out of scope as far as what constitutes an Investment Recommendation follows:

Sell side and buy side: in scope:

- Pre-planned and/or with an intent to distribute.
- Pre-planned where sales people are "plugging" a recommendation to clients, one after the other (sequentially).
- Substantive desk sales notes – recommending an investment strategy.
- Written substantive research.

Sell side and buy side: out of scope:

- Fact-based instrument or issuer: eg term sheet, company results.
- "Generic opinions": eg macroeconomic opinion on hedging strategy. The opinion is on whether or not to hedge using derivatives. No discussion of specific instruments.
- Sector-based opinion: may affect many instruments but not a specific instrument.
- Package/basket transactions: At the moment this is out of scope as the individual security is a component in the package/basket.

Placement of new issues:

- *In scope:* sequential communication, informing the client of a "desk view".
- *Out of scope:* salespersons reading a term sheet to clients when "placing" a new issue.

> "The Regulation came into effect on 3 July 2016.

Buy side:

- *In scope:* recommending a strategy or action with an intent to distribute (pre-planned).
- *Out of scope:* recommendations that are retrospective and fact based in nature: eg fund performance.

Practicalities:

- *On the road sales trips:* if the intention is to give a specific recommendation, then firms should consider providing prepared material for disclosure purposes.
- *Delegated recording of recommendations:* recording of recommendations into database can be delegated: ie someone in the office can update the database when a salesperson is on a sales trip outside the office.

Timeline

The EU Market Abuse Regulation (MAR) final draft Regulatory Technical Standards for Investment Recommendations were submitted by ESMA to the European Commission in September 2015, and adopted by the European Commission in March 2016. Following approval by the European Council and European Parliament, the Regulation came into effect on 3 July 2016.

It is important to note that ESMA has scheduled Level 3 Q&A for some point after MAR Investment Recommendations came into effect on 3 July 2016. No firm Q&A date has yet been announced.

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“Regarding trading, the most important obligations are pre- and post-trade transparency regulations and best execution obligations.

MiFID II/MiFIR

Background: Generally speaking, MiFID II concerns the framework of trading venues and structure in which instruments are traded. MiFIR on the other hand, concentrates on regulating trading venues and structuring its operations: so, “who” the market structures are, “what” they trade and then “how” they trade. Regarding trading, the most important obligations are pre- and post-trade transparency regulations and best execution obligations.

*MiFID II/MiFIR update***:** The outline below sets out our understanding of the regulators’ approach to RTS2 and transparency initiatives and other items high on the MiFID II Working Group list of concerns, such as SFTs (repos) and package transactions. We are now much closer to the MiFID II legislative “end-game”. So there should not be significant changes to the below, apart from tightening them up.

RTS2: The Commission has proposed a *4-year phase-in process* for average daily trades and SSTI percentiles (SSTI = size specific to the instrument). ESMA has accepted this but has strongly recommended an automatic phase-in where there is no chance of a delayed trigger to the next stage.

Commission assessment: Phase-in will not be automatic and move to the next stage without an ESMA approved procedure and a new or amended RTS. So the market cannot proceed to the next stage (of average daily trades or SSTI) until a “green light” is given.

- Commission considers: “necessary to take a more cautious approach to the calibration of the regime in the initial years, gradually building towards ESMA’s proposed calibrations once the data reporting system is effectively up and running and the effects of that regime can be properly assessed.”

ESMA assessment: Phase-in will be automatic and move to the next stage without a new or amended RTS. So the market can proceed to the next stage on an annual basis (average daily trades or SSTI percentiles) automatically unless a “red light” is given, indicating there are significant negative impacts that warrant a halt to the next automatic stage. “Significant” is not defined.

- ESMA considers: “Commission procedure for a regular RTS change risks to result in no meaningful improvement of transparency for many non-equity instruments (bonds), which would run contrary to the objective stated in MiFIR to strengthen transparency and improve the functioning of the internal market. In addition, it creates legal uncertainty and is burdensome for all parties involved.”

SFTs (repos): are exempt from MiFID II regarding pre-trade and post-trade transparency requirements in relation to trade and transaction reporting. It is important to note that repos are in scope for best execution obligations under MiFID II and still seem to be in scope for MiFID II transaction reporting for repos that are exempt under SFTR: eg repo transactions with central banks. For further information, please see the repo and collateral markets section of this Quarterly Report.

Package transactions: The European Parliament accepted the Council drafting on packages. The outline compromise is that a package order should be considered as large in scale (LIS) if at least one of its components is large in scale, unless the package overall is deemed to be liquid.

Timeline: A delay has been approved by the Commission from 3 January 2017 to 3 January 2018 – due to ESMA database IT build.

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Consultation with members on the ICMA Buy-in Rules

ICMA has decided to launch a consultation of its members related to the Buy-in Rules in ICMA’s Secondary Market Rules and Recommendations. This is in response to member feedback suggesting that buying in is becoming increasingly difficult to execute, primarily as a result of the more challenged market liquidity conditions, particularly for credit, emerging markets, and sub-investment grade bonds.

The consultation is designed to inform a review of the Buy-in Rules, which is expected to result in revised rules, designed to improve the efficiency and flexibility of the buy-in process.

Key areas under review will be the timeline of the buy-in process, particularly to the extent that ICMA buy-ins are analogous with other buy-in mechanisms, including repo terminations under a GMRA, and the requirement to appoint a buy-in agent. Furthermore, the new Rules are expected to provide for the possibility of a buy-in auction process, which could be facilitated by trading venues.

While the CSD Regulation provides for a harmonised buy-in mechanism across the European Union, the regulatory technical standards are still to be finalised and are not expected to be enforced until late 2018.

ICMA expects to launch the consultation in 3Q 2016, with the revised Rules in place by the end of 4Q 2016..

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Repo and Collateral Markets

by David Hiscock

Securities Financing Transaction Regulation (SFTR)

As reported in Issue 41 of the ICMA Quarterly Report, on 11 March 2016, ESMA issued a Discussion Paper (DP) on rules under the SFTR. The ICMA ERCC duly submitted, on 22 April 2016, its response to the questions raised in this DP. In responding, the ICMA ERCC focused its efforts on those questions most pertinent to repos, whilst liaising with ISLA, who focused on those questions most pertinent to securities lending, and other relevant trade associations. Along with its specific answers to questions, the ICMA ERCC also took the opportunity to lay out some key overarching comments, under six headings: (i) use clear definitions consistent with current practice; (ii) follow a targeted approach and avoid redundant reporting; (iii) collect information directly from FMIs; (iv) make better use of existing trade matching facilities to improve data quality; (v) ensure consistency with global reporting standards; and (vi) learn the lessons from EMIR implementation. ICMA will continue to discuss these matters with ESMA, with a related Consultation Paper now expected to be published within the next couple of months.

Separately, on 13 April 2016, ICMA, together with AFME, FIA, ISDA and ISLA, jointly published a statement that can be used to help market participants comply with the requirements of Article 15.1(a) of the SFTR. This particular element of the SFTR applies from 13 July 2016 and affects all existing and future title transfer and security collateral arrangements under a variety of financial agreements.

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Net Stable Funding Ratio (NSFR)

On 26 May 2016, the European Commission published a Consultation Paper relating to NSFR. This is a targeted consultation to gather the views of selected stakeholders (in particular financial institutions that could be impacted by the implementation of the NSFR at EU level, associations representing their interests, and supervisory authorities) on specific issues that could be raised by the implementation of the NSFR at EU level.

Already being concerned about this topic, the ICMA ERCC duly submitted its response to this consultation on 24 June 2016. This is quite a comprehensive response, including a paper written to outline the impacts of the NSFR on repo and collateral markets; a series of illustrative impacts; and attempted quantification based upon ICMA ERCC European repo market survey data. In summary, the ICMA ERCC perceives that the cumulative impact of the pressures being imposed on the repo market, most particularly by the Leverage Ratio, is such that it is already a market under significant stress. The impact of the NSFR, if simply adopted exactly as outlined by the BCBS, would create significant additional stress and weaken the effectiveness of the repo market; and, given their interwoven relationship, the collateral market.

Accordingly, the ICMA ERCC considers that, without dropping the worthwhile effort to enhance long-term financing stability through the imposition of NSFR, there are a number of ways in which its details could be calibrated in order to better smooth its effects on repo and collateral markets. To avoid driving essential cash and collateral management activity out of the money markets, which would leave central banks having to intermediate liquidity, the ICMA ERCC believes there is a need effectively to exempt short-term activity from the NSFR imposition of an element of long-term funding costs.

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BCBS: Leverage Ratio

On 6 April 2016, the BCBS released a consultative document (for comment by 6 July) entitled *Revisions to the Basel III Leverage Ratio Framework*, and also published responses to a third set of frequently asked questions (FAQs). Informed by the parallel run period since 2013, by feedback from market participants and stakeholders, and by the frequently asked questions process since the release of the standard in 2014, this consultative document proposes a set of changes which are an important element of the regulatory reform programme that the BCBS has committed to finalise by end-2016.

In the new consultative document, within section III. *Other Proposed Revisions*, section III.5 (at page 10) concerns *Treatment of SFTs*. This recalls the earlier BCBS clarification that "open repos are not eligible for netting" in the BCBS leverage framework. Specific solicitation is made by the BCBS for "further concrete evidence on any adverse impact of the *Basel III Leverage Ratio Framework* on open repos and whether any revisions to the treatment may be warranted (eg so as to allow cash payables and cash receivables associated with open repos to offset each other but not to offset other repos with explicit final settlement dates)." Also of note, within the new FAQs, section 4 on *SFT Exposures* (at page 6) has been expanded (where marked in yellow in the document).

The ICMA ERCC has submitted a response to this consultation. In summary, this highlights that repo and collateral markets lie at the heart of today's financial market system and are vital to its smooth functioning. This has significant implications for both financing, of business and governments, and the effectiveness of financial regulatory measures designed to provide financial stability – each of which will be adversely impacted if the operation of repo and collateral markets becomes impaired. The cumulative impact of the pressures being imposed on the repo market, most particularly by the Leverage Ratio, is such that it is already a market under significant stress.

The ICMA ERCC believes that, without dropping the worthwhile effort to enhance long-term financing stability through the imposition of the Leverage Ratio, there are a number of ways in which its details could be calibrated in order to better smooth its effects on repo and collateral markets. To avoid undesirable consequences from the imposition of the Leverage Ratio, the ICMA ERCC believes there should be further detailed study of possible more detailed specific treatments for special asset types such as holdings of high-quality liquid assets, or in relation to desirable financing activities such as matched book repo facilitation; and has suggested that there is a need to introduce a number of specific refinements, including to exempt central bank reserves from the leverage exposure measure. The benefits of making such market-sensitive adaptations would be felt by borrowers, both corporate and governmental, and investors; and would help underpin the effective functioning of other regulations designed to deliver increased financial stability.

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MiFID II/MiFIR: repo markets

The EU's incoming MiFID and MiFIR rules (published in the *Official Journal* of the EU on 12 June 2014) will govern the trading of securities and, to some extent will impact on repo activities. However, the

There is a need to introduce a number of specific refinements, including to exempt central bank reserves from the leverage exposure measure.

extent to which these rules will apply to repos has been narrowed in two important ways. First, given the requirements being imposed under SFTR, MiFIR transaction reporting obligations will not apply, save in the limited case where the repo counterparty is a member of the ESCB – such SFTs being exempt from SFTR reporting in accordance with SFTR Article 2.3. The ICMA ERCC continues to seek to have this changed so that, notwithstanding the exemption in SFTR, no SFTs should be subject to MiFIR transaction reporting.

Second, on 30 June 2016, an agreed amendment to MiFIR was published in the *Official Journal*. In the first instance this amendment of the rules was prompted by a need to lengthen the timeline for implementation, but importantly as part of the amendment process it was agreed that Article 1 of the amendment should include that: Regulation (EU) No 600/2014 [MiFIR] is amended as follows: (1) in Article 1, the following paragraph is inserted: 5a. Title II and Title III of this Regulation shall not apply to securities financing transactions as defined in point (11) of Article 3 of Regulation (EU) 2015/2365 of the European Parliament and of the Council [SFTR]. The impact of this is that SFTs, the definition of which includes repos, are definitively removed from the pre- and post-trade transparency obligations associated with the MiFIR regime.

It must, however, still be remembered that repos are impacted by incoming best execution rules. Specifically, where they are fulfilling client orders investment firms must publish annual information on the identity of execution venues and on the quality of execution, with SFTs required to be separately reported from client order flow in non-SFTs.

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Money Market Funds Regulation (MMFR)

As further detailed in the ECP market section of this Quarterly Report, there are now negotiations getting under way to try and reconcile the agreed views of the European Commission, Parliament and Council, in order to formulate the final text of the incoming EU MMFR.

The Commission's 2013 proposal included that reverse repos should be eligible investments for MMFs, but specifically did not allow MMFs to enter into any repos, securities lending agreements or securities borrowing agreements. Detailed proposals for eligible reverse repos include that the MMF has the right to terminate the agreement at any time upon a notice of maximum two working days; that the market value of the assets received as part of the reverse repo is at all times at least equal to the value of the cash given out; and that the assets received by the MMF are themselves eligible money market instruments. In addition, the aggregate amount of cash provided to the same counterparty of a MMF in reverse repos shall not exceed 20% of its assets.

The Parliament's 2015 stance broadly followed the Commission's approach to reverse repos, save that the 20% limit was cut to 10%. But importantly it was, contrary to the Commission, proposed that MMFs should also be able to engage in repos – provided that the assets used as collateral are not sold, re-invested or pledged; the repo is used on a temporary basis and not for investment purposes; the MMF has the right to terminate the repo at any time upon giving notice of no more than two working days; and the cash received by the MMF as part of repos does not exceed 10% of its assets and, save in accordance with detailed specified rules, is not transferred, re-invested or otherwise re-used.

Encouragingly, the Council's position, as now confirmed in June 2016, also contemplates that MMFs can engage in repos as well as reverses (but still not in securities lending or borrowing). The conditionality attached to make such repos and reverses eligible for MMFs is broadly equivalent to that reflected in the Parliament's text, save that the Council has followed the Commission's proposal that the limit on reverses be set at 20%. Whilst there is much yet to be agreed in finalising the MMFR, the extent of commonality in the Parliament and Council texts suggests that it is unlikely to be these detailed rules for MMFs' involvement in repos and reverses which will delay the negotiations

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Macroprudential considerations

Systemic Risk in Clearing Houses: Evidence from the European Repo Market is a working paper published by the ESRB on 2 May 2016. It considers the question: how do crises affect CCPs? The authors focus on CCPs that clear and guarantee a large and safe segment of the repo market during the euro area sovereign debt crisis. They start by developing a simple framework to infer CCP stress, which can be measured through the sensitivity of repo rates to sovereign CDS spreads. Such sensitivity jointly captures three effects: (i) the effectiveness of the haircut policy; (ii) CCP member default risk (conditional on sovereign default); and (iii) CCP default risk (conditional on both sovereign and CCP member default). The data show that, during the sovereign debt crisis of 2011, repo rates strongly respond to movements in sovereign risk, in particular for Greece, Ireland, Italy, Portugal and Spain, indicating significant CCP stress. The authors' model suggests that repo investors behaved as if the conditional probability of CCP default was very large.

Published by the BIS, on 30 May 2016, *Mobile Collateral Versus Immobile Collateral* is a working paper by Gary Gorton and Tyler Muir. The authors present that pre-crisis financial architecture was a system of mobile collateral. Safe debt, whether government bonds or privately produced bonds, ie asset-backed securities, could be traded, posted as collateral, and rehypothecated, moving to its highest value use. Since the financial crisis, regulatory changes to the financial architecture have aimed to make collateral immobile, most notably with the BCBS Liquidity Coverage Ratio for banks. The authors evaluate this immobile capital system with reference to a previous regime, which had this feature: the US National Banks Era.

Published by the BIS, on 1 June 2016, *The Collateral Trap* is a working paper by Frederic Boissay and Russell Cooper. The authors explain that active wholesale financial markets help reallocate deposits across heterogeneous banks. Because of incentive problems, these flows are constrained and collateral is needed. Both the volume, the value, and the composition of collateral matter. The authors make a distinction between "outside collateral" and "inside collateral". The use of inside assets, such as loans, creates a "collateral pyramid", in that cash flows from one loan can be pledged to secure another. Through collateral pyramids the financial sector creates safe assets, but at the cost of exposing the economy to systemic panics. Outside collateral, such as treasuries, serves as foundation of, and stabilises, the pyramid. There is a threshold for the volume of treasuries, below which investors panic, the pyramid collapses, and there are not enough safe assets to support wholesale market activity; a situation that the authors call the "collateral trap".

On 6 June 2016, the ESRB held an international conference on the macroprudential use of margins and haircuts. The keynote speech, given by Vítor Constâncio, Vice President, ECB, includes proposals for macroprudential tools to be used for controlling haircuts and margins across SFT (and derivative) markets.

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Repo in Africa

ICMA has been working with a number of jurisdictions worldwide to assist in the development of their respective repo markets. ICMA's focus has been on providing training of regulators and market participants to give a better understanding of the repo market and the GMRA. Richard Comotto, of the ICMA Centre, the author of the ICMA biannual repo survey and several other papers on the repo and collateral market commissioned by ICMA, has been delivering the training.

In addition to working with central banks and authorities in Eastern Europe and across Southeast Asia, ICMA has been active in its support of the Kenyan and Nigeria markets.

In Kenya, ICMA has established a cooperation with Frontclear, a development finance company, focused on catalysing stable and inclusive access to interbank markets for local financial institutions in emerging markets and developing countries. Frontclear has so far sponsored two ICMA workshops in Nairobi, one was delivered for the domestic commercial banks and the other for the Kenyan Capital Market Authority, the Central Bank of Kenya, the National Treasury and domestic commercial banks. The latter of the workshops, which was held in June, was organised by the International Finance Corporation. There is currently no true repo market in Kenya.

In Nigeria, FMDQ is the main debt capital securities exchange of the country and combines the functions of an exchange and an SRO. FMDQ has been tasked to lead the structural reforms to further develop the Nigerian repo market, which currently remains as a wholesale market dominated by banks and discount houses and practically inaccessible to other financial market participants. ICMA has been providing technical assistance to FMDQ and a training workshop is being scheduled to take place later in the year. FMDQ is a member of ICMA.

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Asset Management

by Patrik Karlsson and Dr. Nathalie Aubry-Stacey

Covered bonds

Following the European Commission consultation process on covered bonds, which concluded in early January, and a conference on covered bonds in February, it seems that the Commission's drive for harmonisation is losing some steam. As a result, it is unlikely that the Commission will publish anything on covered bonds in 2016. At the last European Covered Bond Council (ECBC) conference organised in Copenhagen in April, both the ECB and the CBIC stressed that they would like to see the ECBC continue with its own initiatives rather than slow down because of the Commission's delay and, for example, continue the implementation of the Harmonised Transparency Template (HTT).

> "It is unlikely that the Commission will publish anything on covered bonds in 2016.

In the absence of enhanced rules on mandatory pool disclosure on a Europe-wide basis from the European Commission, industry-led initiatives are therefore essential to the continued good operation and standing of the covered bond market. CBIC members had welcomed the significant progress made to date by the Covered Bond Label Committee on the HTT, viewing this as a very positive development and a strong response to the call by the CBIC in 2012 for enhancements to covered bond pool transparency.

The CBIC believes that that Covered Bond Label is indeed a qualitative and quantitative market database, as described in the Covered Bond Label Convention – as long as all Covered Bond Label holders have a compliant HTT on their website by the end of 2016. In the 2015 Press Release, '*Covered Bond Label Issuers Agree Common Harmonised Transparency Template*', it is noted that "the Label […] is based on […] investors' due diligence, thus significantly enhancing comparability and convergence across covered bond jurisdictions". The regular review by investors is part of the CBIC's commitment to enhance transparency in the covered bond market and also to its support and constructively critical assessment of market-led initiatives, ensuring their success.

To date 14 National Transparency Templates have been published and 77 issuers have provided information on 91 labelled cover pools. At this stage, CBIC counted 25 HTT templates (32% of the overall covered bond label population), out of which one could not be easily accessed and three were in "pdf" format. Therefore, the compliant implementation rate is at around 27% at this stage (the last template was accessed on 17 May 2016) – nearly half way through the first implementation year.

Many members of the CBIC have commented on how useful this tool is to them as they undertake due diligence on their covered bond investments and potential future investments. Needless to say, an increase in the number of templates, issuers and pools covered would significantly enhance the efficacy and credibility of the tool.

Our members noted that they value the timeliness and integrity of data and ease of access to the data. However, for the HTT to be of real value, CBIC believes that all covered bond label issuers should make up-to-date HTTs easily available, in excel format, on their website. Some members suggest that concrete deadlines should be set and publicised and, if such deadlines are not met, that there should be a commitment that issuers will no longer be Covered Bond Label-compliant.

However, the fact that the HTT is to be reviewed and enhanced on a yearly basis will allow investors to evaluate its effectiveness and to provide comments from members on possible features to add and refine in the template in future. We will specifically ask for more transparency regarding certain structures, such as conditional pass-through that seem to be more and more prevalent in the market.

The ECBC reviewed CBIC comments on the HTT at their Steering Committee, and welcomed the comments and diligence of investors. The CBIC conference held on 8/9 June 2016 reviewed the harmonisation theme with more than 200 participants – the ECBC confirmed progress with the implementation of the HTT.

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STS securitisation

The debate on the European Commission's proposal on Simple, Transparent and Standardised (STS) Securitisation continues. Since the previous report in the ICMA Quarterly Report, the European Parliament has made some progress in its deliberations on the proposal, but the process is considerably slower than industry had hoped when the Commission issued its proposal and the Council swiftly approved its version last year.

In February, the *rapporteur,* Paul Tang, MEP (S&D, Netherlands), announced a much slower timetable for the European Parliament in its deliberations on the STS proposal, suggesting that it would not reach a view until November 2016, meaning that a final agreement will not be achieved until early 2017 at the earliest.

The *rapporteur* issued his first report on 6 June. The report contained a number of difficult proposals for industry. The headline change is to the risk retention requirement, raising it to 20 % instead of the current 5%. The *rapporteur* also proposes to publish investor holdings, which would be tricky for investors in an OTC market. Furthermore, the *rapporteur* bans any use of third parties in the STS certification process, a key issue for investors.

> **The process is considerably slower than industry had hoped.**

Other MEPs are in the process of tabling their own amendments by 20 July and, once the Parliament is back from the summer break, will start considering compromise amendments in September. Furthermore, the impact of Brexit on the process must also be assessed.

Meanwhile, given the very large degree of consensus on the industry side (sell side, buy side and borrowers) that securitisation should be revived and STS securitisation is a good way of doing it, sell and buy-side organisations have set up a joint European Securitisation Coordination Group. The aim of the group is to coordinate efforts and to exchange intelligence. There will also be an effort to coordinate the proposition of amendments.

While the STS proposal is being delayed, this is having a knock-on effect on the crucial proposal to revise capital requirements for insurers under Solvency II. While bank capital requirements have been proposed to CRR, the process for amending Solvency II has not yet begun. This is particularly frustrating for investors as insurers have been traditional investors in ABS. The main benefit of STS securitisation is the capital treatment that improved calibration in Solvency II would give.

The Commission has indicated that it would launch the capital changes for securitisation in Solvency II when the negotiations on the STS legislation is close to political agreement in trilogue. In practice, this means that the proposal could be delayed until early 2017, seriously delaying any return of insurers to ABS as an asset class and undermining the objectives of CMU.

The AMIC Working Group is preparing, in coordination with other buy-side bodies, an "investor narrative" document to re-emphasise why securitisation is important for investors.

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Systemic risk in asset management

The Financial Stability Board (FSB) published on 22 June 2016 for public consultation, *Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities*. This Consultation Paper follows previous work on designation of systemically risky asset managers in 2014 and 2015. AMIC has strongly welcomed this new focus on activities instead of entities.

The FSB consultation sets out 14 proposed policy recommendations to address the following structural vulnerabilities from asset management activities that could potentially present financial stability risks:

- liquidity mismatch between fund investments and redemption terms and conditions for fund units;
- leverage within investment funds;
- operational risk and challenges in transferring investment mandates in stressed conditions; and
- securities lending activities of asset managers and funds.

The FSB states that, among these four structural vulnerabilities, issues associated with (i) liquidity mismatch and (ii) leverage are considered key vulnerabilities. The recommendations for liquidity mismatch focus on open-ended funds (public and private, including exchange-traded funds but excluding money market funds). Those for leverage are meant to apply to all types of funds that may use leverage (which may arise through borrowings or through the use of derivatives). Meanwhile, recommendations for operational risk focus on asset managers that are large, complex, and/or provide critical services, and those for securities lending activities focus on asset managers' agent lender activities (ie lending of securities of which an entity is not the beneficial owner), in particular their provision of indemnities to clients.

On the same day, the International Organization of Securities Commissions (IOSCO) issued a statement on its initiative regarding the priorities for addressing data gaps related to the asset management sector. The FSB intends to finalise policy recommendations by the end of 2016, many of which will be put into operation by IOSCO through its guidance to the market.

The AMIC Fund Liquidity Working Group will analyse the consultation and respond to it. The Working Group will use as a basis much of the work that went into the report issued in April on fund liquidity risk management.

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Bail-in: buy-side concerns

It was reported in the Second Quarter 2016 edition of this Quarterly Report that members of the Steering Committee of the ICMA Bail-In Working Group (BIWG) were to meet with members of the Financial Institution Issuer Forum in order to assess the current issuer and buy-side positions on bail-in risk assessment and drivers of risk appetite, with a view to presenting a joined-up approach to national regulators as well as to the ECB and others. These efforts are continuing in the respective groups, with the BIWG having met most recently in early July to develop its thinking on the issue. Beyond this, the bail-in mechanism, having only been in operation since 1 January 2016, remains – and is likely to remain – the focal point of much debate across the industry, with the position of the BIWG being represented by its chair and other members of the BIWG.

Meanwhile, members of the BIWG were interested to note comments from Danièle Nouy, Chair of the Supervisory Board of the ECB, in a letter to members of the European Parliament, all of which largely reflect and align with the points articulated by the BIWG in a letter to the ECB in July 2015. This includes, in particular, the importance of investor awareness of the risks attached to any investment in bank securities (notably subordinated instruments or unsecured bonds), the importance of the bail-in tool being applied without causing instability in the system and the problem of non-performing exposures in the euro area banking sector (as to which, the Single Supervisory Mechanism is currently taking stock of the approaches to non-performing loan resolution in the euro area countries, with the aim of fostering a more consistent supervisory approach).

There is not yet full, consistent or clear methodology on the manner in which subordination of bail-inable debt will be achieved across EU Member States; whether by structural, contractual or statutory subordination. Although the risks to bondholders will be broadly similar, at least in terms of the probability of bail-in, an inconsistent, patchwork approach poses a significant challenge for the buy side in terms of predictability, adds complexity to the task of resolving cross-border banks and may give rise to multiple legal challenges should the bail-in tool be exercised.

In this regard, the BIWG has suggested that the future development and success of the market for regulatory capital instruments would be best served by a high degree of standardisation and homogeneity, including a common framework for achieving subordination.

A recent issue by Nykredit of Senior Resolution Bonds is one example of an intermediate asset class which sits between regulatory capital and senior unsecured debt. Although not BRRD-driven (mortgage banks in Denmark are exempt from the bail-in tool and are instead subject to a specific debt buffer requirement under local law), this may signal a move towards issuance of similar separate tier of debt which would sit alongside MREL-eligible, senior unsecured issuance by banks.

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Other regulatory developments

At the last AMIC Executive Committee meeting, which was held in London at the beginning of June, two regulatory developments were discussed by Executive Committee members. The AMIC will work with other trade associations on these topics.

Cross-border distribution of investment funds

The European Commission's consultation on cross-border distribution of investment funds was issued a week before the AMIC meeting. The consultation is one of the first concrete action items coming from the cumulative impact assessment exercise by the Commission. The consultation asks a number of questions about national marketing rules that inhibit the cross-border market of investment funds. And the consultation is not limited to just UCITS funds, but to all EU fund structures (ie AIFs, ELTIFs, EuVeCas and EuSEFs).

The consultation is quite detailed. The Commission is looking for very specific market examples of obstacles. Furthermore, the head of DG FISMA's asset management unit, Sven Gentner, is intending to tour Europe to discuss obstacles with industry bodies. There are a number of practical obstacles that are not in the Commission's remit to change (eg tax), but cooperation between Member States should be attempted so as to make progress on this file. To this end, the Commission is hoping that industry can provide appropriate further evidence.

The AMIC Secretariat will monitor progress and will coordinate with other trade associations.

A European framework for loan funds

In its April *Opinion on a European Framework for Loan Origination by Funds*, ESMA sets out its view on the necessary elements for a common European framework, taking into account the different frameworks currently in place in several Member States. ESMA advocates that a common approach at EU level would contribute to a level playing field for stakeholders, as well as reducing the potential for regulatory arbitrage, and it might in turn facilitate the take up of loan origination by investment funds, in line with the objectives of Capital Markets Union.

Specifically, ESMA promotes some form of mandatory authorisation for loan originating Alternative Investment Funds (AIFs). ESMA suggests that the Commission should look at authorisation being requested for funds and/or managers. The international debate around banning any entity except a bank to create money has led to calls for zero leverage in loan funds. The European Commission has not made any statement yet, but a restrictive regime would needlessly hold back non-bank loan origination and undermine CMU goals.

The Opinion states that the Commission intends to consult on the elements of a European framework on loan origination in the second quarter of 2016. ESMA is of the view that the elements presented in its Opinion should ideally form part of a harmonised European framework on loan origination. This could be achieved in different ways, eg through a legislative proposal or by way of an ESMA instrument supplementing the AIFMD.

AIMA has set up the Alternative Credit Council (ACC) to represent members and interested industry participants on loans and synthetic finance. Much of the advocacy of the ACC has been directed towards Member States, as national frameworks for loan origination has a significant impact on any EU ideas. The ACC has started publishing an annual survey on funds' loan origination, called *Financing the Economy: The Role of Alternative Asset Managers in the Non-Bank Lending Environment*.

AMIC members will discuss their position in advance of the European Commission consultation, and will share information with the ACC.

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International Regulatory Digest

by David Hiscock and Alexander Westphal

G20 financial regulatory reforms

On 6 April 2016, the BCBS released a consultative document (for comment by 6 July) entitled *Revisions to the Basel III Leverage Ratio Framework*, and also published responses to a third set of frequently asked questions (FAQs). Informed by the parallel run period since 2013, by feedback from market participants and stakeholders, and by the frequently asked questions process since the release of the standard in 2014, this consultative document proposes a set of changes which are an important element of the regulatory reform programme that the BCBS has committed to finalise by end-2016.

The proposed revisions cover the following issues:

- to measure derivative exposures, the BCBS is proposing to use a modified version of the standardised approach for measuring counterparty credit risk exposures (SA-CCR) instead of the Current Exposure Method (CEM);
- to ensure consistency across accounting standards, two options are proposed for the treatment of regular-way purchases and sales of financial assets;
- clarification of the treatment of provisions and prudential valuation adjustments for less liquid positions, so as to avoid double-counting; and
- alignment of the credit conversion factors for off-balance sheet items with those proposed for the standardised approach to credit risk under the risk-based framework.

The BCBS also sought comment on an additional Leverage Ratio requirement applicable to G-SIBs. The final design and calibration of the proposals will be informed by a forthcoming comprehensive quantitative impact study.

On 11 April 2016, the BCBS issued its *Tenth Progress Report* on adoption of the Basel regulatory framework, which sets out the adoption status of Basel III standards for each BCBS member jurisdiction. As of March 2016, all 27 BCBS member jurisdictions have final risk-based capital rules, LCR regulations and capital conservation buffers in force. Further, 24 member jurisdictions have issued final rules for the countercyclical capital buffer and 23 have issued final or draft rules for their domestic SIBs framework. With regard to the G-SIBs framework, all BCBS members that are home jurisdictions to G-SIBs have the final framework in force. Member jurisdictions are now turning to the implementation of other Basel III standards, including the Leverage Ratio and the NSFR.

A communiqué was issued following the G20 Finance Ministers and Central Bank Governors meeting held, on 14-15 April 2016, in Washington D.C. Paragraph 6 of the communiqué specifically concerns ongoing financial regulatory reforms and includes the following:

- We reiterate our commitments to finalizing remaining core elements and support the timely, full and consistent implementation of our agreed financial sector reform agenda, including the Basel III and TLAC standards.
- We also reiterate our support for the work by the BCBS to refine elements of the Basel III framework

to ensure its coherence and maximize its effectiveness without further significantly increasing overall capital requirements across the banking sector.

- We will continue to enhance the monitoring of implementation and effects of reforms to ensure their consistency with our overall objectives, including by addressing any material unintended consequences.
- We look forward to the coordinated work by the IMF, FSB and BIS to take stock of international experiences with macroprudential frameworks and tools, to help promote effective macroprudential policies and report back by our next meeting;
- We welcome the FSB's work in cooperation with other standard setting bodies to assess holistically the extent, drivers and possible persistence of shifts in market liquidity across jurisdictions and asset classes and consider policy measures if necessary.
- We look forward to planned public consultation in mid-2016 on policy recommendations to address structural vulnerabilities associated with asset management activities.
- We look forward to the FSB peer review report on country-specific implementation of the FSB policy framework for shadow banking entities, and call upon the membership to address identified gaps and on the FSB to evaluate the case for further policy recommendations if appropriate.
- We reiterate our commitment to expediting implementation of the PFMIs, and to progressing on the work to enhance CCP resilience, recovery planning and resolvability, including on cross-border cooperation arrangements, and look forward to the report by the FSB in September.

On 21 April, the BCBS issued standards for *Interest Rate Risk in the Banking Book* (IRRBB), which are expected to be implemented by 2018. These standards revise the BCBS's 2004 *Principles for the Management and Supervision of Interest Rate Risk*, which set out supervisory expectations for banks' identification, measurement, monitoring and control of IRRBB as well as its supervision.

The key enhancements to the 2004 Principles include:

- more extensive guidance on the expectations for a bank's IRRBB management process;
- enhanced disclosure requirements;
- an updated standardised framework; and
- a stricter threshold for identifying outlier banks.

The IRRBB standards reflect changes in market and supervisory practices since the Principles were first published in 2004, which is particularly pertinent in light of the current exceptionally low interest rates in many jurisdictions.

On 11 May, IOSCO opened the public sessions of its Annual Conference in Lima focusing on SME financing, investor protection and education, and the opportunities and challenges of new financial technologies (Fintech). This public conference comes at the conclusion of IOSCO's private meetings in which members discussed responses to the challenges currently facing markets regulators. During the four-day meeting, the IOSCO Board, the Growth and Emerging Markets (GEM) Committee, the four Regional Committees and the Affiliate Members Consultative Committee (AMCC) discussed policy initiatives to strengthen securities market resilience and ensure that securities markets continue to be sustainable sources of finance.

We welcome the FSB's work in cooperation with other standard setting bodies to assess holistically the extent, drivers and possible persistence of shifts in market liquidity across jurisdictions and asset classes and consider policy measures if necessary.

“Establish a systematic process involving all relevant domestic authorities to assess the shadow banking risks posed by non-bank financial entities or activities.

In particular, members discussed how best to make use of the expertise and knowledge of IOSCO’s diverse membership, including measures to further the integration and enhance the participation of GEM Committee members. On enforcement cooperation, IOSCO’s Presidents Committee approved the text of an Enhanced MMoU on cooperation and the exchange of information. This Enhanced MMoU, which is aspirational in nature, provides for the additional powers that IOSCO believes are necessary for its member regulators to ensure their continued effectiveness in deterring cross-border misconduct and fraud in securities markets. It builds on the success of the current MMoU on cooperation and exchange of information, while taking into account technological and regulatory developments since the launch of the original MMoU in 2002. It was resolved that arrangements for implementation of the enhanced MMoU will be developed by the Board with a view to approval by the Presidents Committee by the end of 2016.

On policy work, the IOSCO Board progressed its work on asset management by focusing on liquidity risk management and leverage. Additionally, it considered how to address gaps in asset management data collected by securities regulators, and will publish a statement in this regard shortly. In other key policy areas, the IOSCO Board heard updates on work on CCP resilience and recovery, market conduct in wholesale markets, and revisions to IOSCO’s Objectives and Principles of Securities Regulation and supporting Methodology. On the issue of infrastructure finance, the Board agreed to establish a working group comprised of Board members from both advanced and growth and emerging markets that will engage with development banks, institutional investors and other stakeholders to discuss issues relevant to market based finance for infrastructure development.

On identifying and addressing emerging risks, the Board discussed the issue of liquidity in securities markets, with a particular focus on liquidity in corporate bond markets; and will shortly publish a consultation paper on corporate bond market liquidity and take up further work on corporate bond market transparency. The Board also discussed its work on cyber resilience and Fintech, agreeing to consider different mechanisms for securities regulators to share and gather information on cyber risk and cyber security issues that are relevant to securities regulators across its membership; and receiving an update on IOSCO work on the potential impact of Fintech and digitalization on securities markets and regulation.

On 25 May, the FSB published its thematic peer review on the progress made by FSB member jurisdictions in implementing its *Policy Framework for Strengthening Oversight and Regulation of Shadow Banking Entities*. This peer review concludes that, notwithstanding the progress made, implementation of the Policy Framework remains at a relatively early stage. More work is needed to ensure that jurisdictions can comprehensively assess and respond to potential shadow banking risks posed by non-bank financial entities, and support FSB risk assessments and policy discussion.

The peer review makes a number of recommendations to FSB jurisdictions to implement fully the Policy Framework. These are:

- establish a systematic process involving all relevant domestic authorities to assess the shadow banking risks posed by non-bank financial entities or activities;
- address data gaps to be able to better assess the potential financial stability risks posed by non-bank financial entities or activities;
- remove impediments to cooperation and information-sharing between authorities, including on a cross-border basis; and
- review and enhance public disclosures by non-bank financial entities as necessary to help market participants understand the shadow banking risks posed by such entities.

The FSB will continue to monitor jurisdictions’ implementation of the Policy Framework, including the above recommendations.

On 16 June, the BCBS published reports assessing the implementation of the BCBS's frameworks for G-SIBs and D-SIBs. These evaluations cover the five jurisdictions that are currently home to G-SIBs: China, the EU, Japan, Switzerland and the US. This is the first assessment to be conducted on a cross-jurisdictional basis, with these five jurisdictions being simultaneously assessed against the Basel framework. These reports form part of a series of publications on BCBS members' implementation of Basel standards under the BCBS's Regulatory Consistency Assessment Programme (RCAP). The RCAP assesses the consistency and completeness of a jurisdiction's adopted standards and the significance of any deviations from the Basel framework; but does not take account of a jurisdiction's bank supervision practices, nor evaluate the adequacy of regulatory capital for individual banks or a banking system as a whole.

The third G20 Finance and Central Bank Deputies meeting under the Chinese Presidency was held in Xiamen, on 22-23 June 2016. Deputies discussed issues including global economy, framework for strong, sustainable and balanced growth, investment and infrastructure, international financial architecture, financial sector reform, international tax, green finance, climate finance and anti-terrorist financing; and general consensus was reached on this year's major expected outcomes under the G20 finance track. Related outcomes will be submitted to the third G20 Finance Ministers and Central Bank Governors Meeting to be held in Chengdu, on 23-24 July, for approval.

On 26 June, the BIS published its 86th Annual Report. In this report the BIS writes that there is an urgent need to rebalance policy in order to shift to a more robust and sustainable global expansion and address accumulated vulnerabilities, calling for prudential, fiscal and structural policies to play a greater role working alongside monetary policy. The BIS identifies a risky combination of unusually low productivity growth, historically high global debt and shrinking room for policy manoeuvre, which leaves the global economy highly exposed, not least to shocks and political risks. The BIS notes that the structure of taxes and subsidies could be adjusted to remove the bias towards debt accumulation, for example by eliminating the tax advantage of debt over equity, and the quality of public spending could be improved by focusing more on investment. It also states that safer and stronger banks will contribute to a more resilient economy since better capitalised banks lend more and stronger market-makers mean more robust market liquidity.

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European financial regulatory reforms

On 25 April, the European Commission published its first CMU status report, in which it takes stock of the progress made in the first six months since the adoption of the CMU Action Plan. The report includes sections on steps taken since adoption of the CMU Action Plan, key initiatives planned by end-2016 and preparation of other CMU actions in 2017 and 2018; and it indicates that first measures are already having an impact on the ground. New rules have just entered into force to support investment by insurers and reinsurers in infrastructure projects. The Commission's legislative proposal to restart securitisation markets in Europe was agreed in record time by Member States in December 2015; and a proposal was also presented to simplify prospectus requirements and reduce burdens for companies issuing shares and bonds – the Commission hopes that these proposals will be agreed swiftly by the co-legislators.

The Commission has also carried out a cumulative assessment of the financial services legislation – the Call for Evidence – to check that its legislative framework is working to support growth across the EU. And the work continues: the Commission has launched a public consultation on business restructuring and insolvency in order to tackle some of the longer-term issues that are holding back jobs and growth in the EU; the Commission will soon take further actions to promote personal pensions; and the Commission will shortly publish a report on the development of crowdfunding markets in the EU. The Commission will also propose measures to stimulate European venture capital markets, including a revision of the venture capital legislation and work on a venture capital "fund of funds"; and they will also launch a public consultation to gather views on how the passporting rules for the cross-border distribution of investment funds can be improved.

In parallel with the CMU status report, the Commission also published a new edition of the *European Financial Stability and Integration Review* (EFSIR), which this year focuses on CMU and identifies some promising developments in European capital markets. The EFSIR builds on the economic analysis that had supported the publication of the CMU Action Plan.

Publication of the EFSIR comes alongside a one day joint conference of the Commission and the ECB, *Completing European Financial Integration: What Next?* The ECB's published contribution towards this is the 2016 edition of its report on *Financial Integration in Europe*, which indicates that the financial re-integration trend has moderated, but

Be more proportionate in the way legislation is applied, more cautious before doing anything that might reduce liquidity, and more ambitious about reducing reporting.

that an ambitious CMU will boost the benefits of integration. The report highlights a series of policy actions that support the financial re-integration trend. In addition to the ECB's expansionary monetary policy, the SRF became operational this year; and ECB Banking Supervision is addressing remaining cross-country heterogeneities in the regulatory framework. Looking ahead, the ECB emphasises that CMU and all the other steps proposed in last year's Five Presidents' Report need to be pursued with determination in this context. The ECB's report makes a strong case for strengthening Europe's more bank-oriented financial system by better developing and integrating capital markets, notably in the equity space. The analysis explains how this can improve the system's resilience, enhance cross-country risk-sharing and improve the financing options of firms and households.

On 17 May, the Commission hosted a public hearing, in Brussels, on its Call for Evidence. This public consultation exercise was launched in September 2015 to collect feedback and empirical evidence on the benefits, unintended effects and consistency of the EU regulatory framework for financial services. The public hearing was an opportunity for stakeholders to further substantiate their respective submissions and to discuss the initial results of the consultation.

At the hearing, Commissioner Hill gave a keynote speech, in which he said: "We'll complete our analysis by the summer, by which time we should be clearer on what further actions are needed. But the evidence you've already provided has already given us a lot of useful intelligence. I want to use every single one of the 100 upcoming reviews already planned to make sure we have the best possible legislation, and where there's enough evidence, to address your concerns. EMIR and CRR were two areas mentioned frequently and the reviews we are undertaking of them this year are going to be particularly important. I want to be more proportionate in the way legislation is applied, more cautious before doing anything that might reduce liquidity, and more ambitious about reducing reporting and disclosure requirements where it's appropriate." To inform the hearing, the Commission services published a summary of the 288 responses received from respondents based in 25 different countries, providing a factual overview of the contributions received and of the examples provided by respondents.

Overall, stakeholders did not dispute the reforms of recent years and many expressed support, highlighting the benefits of the new rules. But the Call for Evidence was also welcomed as giving all interested parties the opportunity to assess the potential interactions, overlaps and inconsistencies between different pieces of legislation. Of the 15 pre-defined topics for consultation, most replies related to unnecessary regulatory constraints on financing (issue 1), proportionality (issue 4), excessive compliance costs and complexity (issue 5), reporting and disclosure obligations (issue 6) and overlaps, duplications and inconsistencies (issue 12).

While respondents referred to all the main legislative acts in financial services, most replies concerned CRR/CRD IV and MiFID/R, followed by EMIR as well as AIFMD, UCITS and Solvency II. The majority of examples related to single pieces of legislation, but respondents also provided a significant number of examples relating to a combination of pieces of legislation. Respondents provided a number of examples and descriptions of where the rules are perceived to be inconsistent, overlapping or duplicative (eg reporting and disclosure requirements, definitions).

Limited specific information was provided as regards the compliance costs or the wider market impacts of these inconsistencies or overlaps. Similarly, feedback on the market impacts of the different rules (eg their impact on funding or market liquidity or other unintended consequences) was largely qualitative or based on external studies. This may reflect the difficulty of assessing the impact of rules that are very recent (or not yet implemented or adopted). It may also reflect the difficulties inherent in isolating the impact of EU rules from other factors (eg monetary policy, national policy changes, macroeconomic developments) that may also play a significant role.

Want to be more proportionate in the way legislation is applied, more cautious before doing anything that might reduce liquidity, and more ambitious about reducing reporting and disclosure requirements.

A number of market participants (including ICMA, whose response to the Call for Evidence focused on this aspect) argued that specific pieces of legislation and the cumulative impact of certain EU rules have had a detrimental impact on market liquidity, particularly in corporate bond markets. Other respondents questioned whether regulation was responsible for the decline in market liquidity, arguing that other factors play a greater role, and that the evidence of an adverse impact of regulation is unclear. Some public sector respondents cautioned that part of the impact of regulation was intended and reminded of the risks of excessive liquidity before the financial crisis.

On 15 June, ESMA published its Annual Report for 2015, which describes its key accomplishments during the year. In 2015, ESMA has made significant steps in realising its mission of enhancing investor protection and promoting stable and orderly financial markets through a variety of means, namely assessing risks to investors, markets and financial stability, creating a single rulebook, promoting supervisory convergence and supervising CRAs and trade repositories. On the same day, Annual Reports were also published by EBA and EIOPA.

On 17 June, the European Council published its conclusions on a roadmap to complete the Banking Union. Having taken note of the applicable context, these underline the following key steps:

- Banking regulation proposals of the Commission, including regarding MREL, BRRD, leverage and NSFR, should be put forward as soon as possible and by no later than the end of 2016. On that basis, the Council will start technical work immediately in view of a swift implementation; and mindful of the importance of considering European specificities when implementing global regulatory standards in the EU.
- On the common backstop for the SRF, the Council takes note of the intention of Member States to start work in September 2016 if and when all participating Member States have fully transposed the BRRD. In this context, the Council will also take stock of the establishment of the bridge financing arrangements, noting that participating Member States are committed to sign the Loan Facility Agreement by that time; and reaffirm the need to have the common backstop fully operational at the latest by the end of the transition period.
- On the regulatory treatment of sovereign exposures, the Council agrees to await the outcomes of the Basel Committee and then to consider possible next steps in the EU context.
- On a European Deposit Insurance Scheme (EDIS), the Council will continue constructive work at technical level, with negotiations at political level to start as soon as sufficient further progress has been made on risk reduction measures mentioned above. In this context, the Council takes note of the intention of Member States to have recourse to an IGA when political negotiations on EDIS start.
- The Council will assess annually the progress made on the above mentioned measures towards completing the Banking Union.

On 30 June, it was announced that the Slovak Government has approved the Programme of the Slovak Presidency of the Council of the EU, which runs for the second half of 2016. The Programme is based on four priorities: an economically strong Europe, a modern single market, sustainable migration and asylum policies, and a globally engaged Europe. The themes which will be at the forefront of the Slovak Presidency have three interconnecting principles: achieving tangible results, overcoming fragmentation, and focusing on the citizen.

According to this Programme, within the ECOFIN agenda the Presidency will pay particular attention to the measures necessary to complete EMU following the Five Presidents' Report, to combat tax fraud and evasion and to increase tax transparency. In order to support investment in the EU, the Presidency will strive to make maximum use of and strengthen the potential of the European Fund for Strategic Investments. The Presidency will also pursue discussions on the measures necessary to create CMU, to complete Banking Union with particular emphasis on its second and third pillar, and to simplify the rules of the Stability and Growth Pact.

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Financial benchmarks

On 28 April, the European Parliament approved by a large majority in the plenary session the adoption of the proposed Regulation on financial benchmarks – the Benchmarks Regulation (BR) – following a political agreement by the Parliament and the European Council in November 2015. On 17 May 2016, the Council also formally adopted these new rules; and the BR was subsequently published in the EU *Official Journal* on 29 June 2016. As per Article 59, the BR then entered into force on the following day and, subject to a specified list of exceptional articles which are immediately applicable (and Article 56 on amendments to the Market Abuse Regulation, which applies from 3 July 2016), shall apply from 1 January 2018.

The BR will introduce a legally-binding code of conduct for data contributors, requiring the use of robust methodologies and sufficient and reliable data. In particular, it calls for the use of actual transaction input data where possible. But other data may be used if the transaction data is insufficient.

The scope of the BR is broad, although benchmarks deemed to be critical will be subject to stricter rules, including the power for the relevant competent authority to mandate contributions of input data. The BR will not apply to the provision of benchmarks by central banks, and, in certain circumstances, by CCPs and public authorities.

Administrators of benchmarks will have to apply for authorisation and will be subject to supervision by the competent authority of the country in which they are located. If an administrator does not comply with the provisions of the BR, the competent authority may withdraw or suspend its authorisation. Administrators will be required to have in place appropriate governance arrangements and controls to avoid conflicts of interest.

ESMA will coordinate the supervision of benchmark administrators by national competent authorities. For critical benchmarks, a college of national supervisors including ESMA will be set up and take key decisions.

On 27 May, ESMA published a Consultation Paper on draft implementing measures regarding the BR. ESMA is seeking stakeholder's input on draft Technical Advice (TA) it is supposed to develop in order to detail the implementation of the incoming BR. The CP is seeking stakeholder's feedback on the proposed BR framework, including in the following key areas:

- definition of benchmarks;
- measurement of the use of critical and significant benchmarks;
- criteria for the identification of critical benchmarks;
- endorsement of a benchmark/family of benchmarks provided in third countries; and
- transitional provisions.

This ESMA CP was open until 30 June 2016. ESMA will use the feedback received to finalise its technical advice in time for the deadline defined within the mandate received from the European Commission, ie four months after BR's entry into force. A separate consultation will be held on the technical standards ESMA has to develop under the BR, which ESMA shall submit as drafts to the Commission, by 1 April 2017.

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“The BR will introduce a legally-binding code of conduct for data contributors, requiring the use of robust methodologies and sufficient and reliable data.

> **The EBA published a Decision confirming the use of unsolicited credit assessments assigned by certain ECAIs for calculating institutions' capital requirements.**

Credit Rating Agencies

On 1 April 2016, the BCBS published a second report on RWAs in the banking book, as part of its Regulatory Consistency Assessment Programme to ensure full and effective implementation of the Basel III framework. The study examines the variability of RWAs in banks that use internal models to calculate their credit risk regulatory capital requirements. It follows the BCBS's 2013 report, which found considerable variation in average RWAs for credit risk in the banking book, and extends that analysis. The report also describes sound practices relating to banks' independent model validation functions, as observed during the BCBS's engagement with banks in the course of this study.

On 12 April, ESMA published its latest set of semi-annual statistical data on the performance of credit ratings, including transition matrices and default rates. This latest dataset covers the period from 1 July to 31 December 2015 and is available in the Central Rating Repository (CEREP).

On 12 May, the Joint Committee of the ESAs published its Opinion on the European Commission's intention to amend the draft ITS on the mapping of External Credit Assessment Institutions' (ECAIs) credit assessments under the CRR and Solvency II Directive. The Opinion was produced in response to the Commission's proposed amendments to these draft ITS.

The draft ITS were prepared by the ESAs and submitted to the Commission via the Joint Committee in November 2015. In these ITS, the ESAs had particularly proposed "less conservative" quantitative requirements to apply for a phase-in period of three years. Thus, the ECAIs could receive the best mapping based on their past performance, irrespective of how many ratings they have already produced. Upon expiry of the phase-in period, from 2019 onwards, the Joint Committee intended to apply a "more conservative" approach, requiring ECAIs to issue a minimum number of ratings in order to receive the best mapping.

Previously, on 30 March 2016, the Commission informed the Joint Committee of its intention to amend the draft ITS by extending the "less conservative" approach to the mapping of ECAIs. In their Opinion, the ESAs express their disagreement with the Commission's proposal since favouring competition aspects over prudential considerations increases the risk to financial stability and is not in line with the mandate given to the ESAs. The Joint Committee believes that the initial draft ITS represent a good balance of prudential objectives and at the same time sufficiently promote market competition in the credit rating industry.

On 17 May, the EBA published a Decision confirming the use of unsolicited credit assessments assigned by certain ECAIs for calculating institutions' capital requirements. The Decision is part of the Single Rulebook in banking and will ensure regulatory harmonisation across the EU regarding the use of unsolicited credit ratings for determining institutions' own funds requirements.

On 30 June, ESMA announced that it considers the regulatory framework for CRAs of South Africa to be as stringent as EU rules. This decision allows an EU CRA to endorse credit ratings issued by its South African subsidiary or parent company; and such endorsed credit ratings may then be used for regulatory purposes in the EU. In order to facilitate the exchange of regulatory information, and as a precondition to endorsement, ESMA has also entered into a cooperation agreement, effective from 30 June 2016, for the supervision of CRAs with the competent South African authority, the Financial Services Board.

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OTC (derivatives) regulatory developments

On 1 April 2016, IOSCO released an update of its information repository for central clearing requirements for OTC derivatives, which provides regulators and market participants with consolidated information on the clearing requirements of different jurisdictions. First made public by IOSCO in August 2014, the repository sets out central clearing requirements on a product-by-product level, and any exemptions from them. By providing this information, IOSCO seeks to assist authorities in their rule making and help participants comply with the relevant regulations.

On 4 April, ESMA announced that it sees no need to temporarily exclude exchange-traded derivatives (ETDs) from non-discriminatory access to CCPs and trading venues, which will be introduced by MiFID II and MiFIR. MiFIR requires ESMA to assess whether ETDs should be exempted for a period of 30 months from the non-discriminatory access provisions. ESMA's analysis found that open access to ETDs does not create undue risks to the overall stability and orderly functioning of European financial markets. As potential risks relating to open access are already addressed by the legislative frameworks of MiFID II, MiFIR and EMIR, ESMA proposed to the European Parliament and Council not to introduce an ETD specific phase-in regarding the access provisions of MiFID II.

On 5 April, ESMA sent an amended RTS under EMIR for endorsement to the European Commission. This RTS detail the margin period of risk (MPOR) for CCP client accounts, eg the amount of initial margins collected by a CCP. The amended RTS would allow EU-based CCPs to margin on a one-day MPOR basis. This reduces from two-day to one-day the MPOR for gross omnibus accounts and individual segregated accounts for ETDs and securities. Following the US equivalence decision by the European Commission, the amended RTS would provide a level playing field between European and US CCPs of one-day MPOR. The client account structures together with the conditions that they need to respect for the CCPs to margin on a one-day MPOR basis ensure a sufficient level of protection to the CCPs and a greater protection for clients.

Also on 5 April, ESMA published an amended RTS dealing with the access, aggregation and comparison of data across trade repositories, under EMIR. ESMA proposed these amendments in order to ensure higher quality of data and to enhance the access to data by authorities and allow for the comparability and aggregation of data across trade repositories.

On 29 April, ESMA published the results of its first EU-wide stress test exercise regarding CCPs. The exercise is aimed at assessing the resilience and safety of the European CCP sector as well as to identify possible vulnerabilities. The results of the test show that the system of EU CCPs can overall be assessed as resilient to the stress scenarios used to model extreme but plausible market developments. ESMA's stress test solely focused on the counterparty credit risk which CCPs would face as a result of multiple clearing member defaults and simultaneous market price shocks, leaving additional risk dimensions for future such exercises. In addition, ESMA also issued recommendations on how to improve CCPs' internal methodologies.

> **Results of the test show that the system of EU CCPs can overall be assessed as resilient to the stress scenarios used to model extreme but plausible market developments.**

On 26 May, ESMA issued two final draft RTS on indirect clearing under MiFIR and EMIR respectively. The draft RTS clarify provisions of indirect clearing arrangements for OTC and exchange-traded derivatives and help to ensure consistency and that an appropriate level of protection for indirect clients exists. ESMA has sent these draft RTS on indirect clients for endorsement to the European Commission which has three months to accept or reject them. This is followed by a non-objection period by the European Parliament and Council.

On 6 June, ESMA and the US CFTC announced their establishment of a memorandum of understanding (MoU), effective as of 2 June 2016, under EMIR. This MoU establishes cooperation arrangements, including the exchange of information, regarding CCPs which are established in US and authorised or recognised by the CFTC and which have applied for EU recognition under EMIR.

EMIR provides for cooperation arrangements between ESMA and the relevant non-EU authorities whose legal and supervisory framework for CCPs have been deemed equivalent to EMIR by the European Commission.

On 10 June, the European Commission adopted a new set of rules that require certain OTC interest rate derivative contracts denominated in specific European currencies – namely the Norwegian Krone (NOK), Polish Zloty (PLN) and Swedish Krona (SEK) – to be cleared through CCPs. This decision takes the form of a Delegated Regulation and implements the clearing obligation under EMIR; and constitutes the third set of classes to be subject to the clearing obligation. The clearing obligations will enter into force subject to scrutiny by the European Parliament and Council and will be phased in over three years to allow additional time for smaller market participants to comply.

Following the communication, of 9 June 2016, from the European Commission staff and the public communication by the European Commission on the delayed adoption of the Joint draft RTS on risk mitigation techniques for non-CCP cleared OTC derivatives (RTS on bilateral margins), the ESAs published a, 30 June, letter to Commissioner Hill. In this letter the ESAs express their strong concerns with this delay ask that the Commission keep this delay as short as possible.

On 4 April 2016, ESMA issued an update of its Q&A on practical questions regarding EMIR. The updated document includes a new Q&A regarding the population of the "clearing obligation" field in the trade reports. In particular, this Q&A explains how the description of the field should be interpreted, how it should be populated during the frontloading period and how long the counterparties are allowed to report value "X" (standing for "not available"). A further update, issued on 6 June 2016, includes new answers in relation to the clearing obligation, specifically about the self-categorisation that is necessary in order to establish which counterparties belong to which categories. The Q&A also provides clarifications on how counterparties should handle the situation where some of their counterparties have not provided the information on the category they belong to.

On 8 April, ESMA published a new Q&A document on the application of the MiFID to the marketing and sale of financial contracts for difference (CFDs) and other speculative products to retail clients (such as binary options and rolling spot forex). An update to this Q&A was published, on 1 June 2016.

ESMA's list of CCPs authorised to offer services and activities in the EU, in accordance with EMIR, was last updated on 12 May 2016; its list of third-country CCPs recognised to offer services and activities in the EU was last updated on 17 June 2016; its *Public Register for the Clearing Obligation* under EMIR was last updated on 11 May 2016; but its (non-exhaustive) list of CCPs established in non-EEA countries which have applied for recognition has not been updated since 8 January 2016.

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Market infrastructure

ECB: Contact Group on Euro Securities Infrastructures (COGESI)

The latest regular meeting of the COGESI Group was held on 18 February 2016. Among other things, participants reviewed at this meeting a preliminary list of key activities to achieve further harmonisation of collateral management arrangements. COGESI members underlined that harmonisation is important from an operational perspective to move collateral quickly and efficiently across borders to where it is needed, and identified three Priority 1 areas where further work should be undertaken: (i) collateral mobility; (ii) collateral holding and segregation; and (iii) collateral messaging. Accordingly, it was agreed to create three COGESI sub-groups which were tasked to look at the priority issues at stake in more detail. The ICMA ERCC is contributing to all three workstreams, including taking the lead on issue number three. On 28 June 2016 a first COGESI workshop took place in Frankfurt to take stock of the work undertaken by the three sub-streams. The next regular semi-annual COGESI meeting will be held in late November 2016.

ECB: Money Market Contact Group (MMCG)

On 9 June 2016 the MMCG held its latest quarterly meeting. While no documents have been published yet for that meeting, a summary and the presentations of the previous meeting of the Group, held on 15 March 2016, are now available on the group's webpage. During the March meeting MMCG members discussed the main results of the latest quarterly MMCG Euro Money Market Survey and reviewed the latest market developments, in particular following the significant monetary policy decisions by the ECB's Governing Council of 10 March 2016. Members also exchanged views on the distribution and circulation of excess liquidity in the euro area, mainly focusing on regulatory impacts and low money market rates, and how these put constraints on the redeployment and circulation of excess reserves. Besides those discussions, the ECB updated members on some of their relevant work, including (i) developments in the Eurosystem's securities lending arrangements, (ii) the implementation of the ECB's Money Market Statistical Reporting Regulation (MMSR), and (iii) the ongoing reform process in relation to money market benchmarks. The next regular meeting of the MMCG is scheduled for 27 September 2016.

ECB: Bond Market Contact Group (BMCG)

The BMCG, in which ICMA is represented through its Chief Executive, last met on 21 June 2016 in

Frankfurt. The agenda for the meeting included, as usual, an exchange of views on the main recent developments and the outlook for European bond markets. Furthermore, the Group discussed the impact of Solvency II on European bond markets, as well as the potential implications for the market of the UK leaving the EU. Under other items, BMCG members focused among other things on the impact of the recent regulation on repo market activity from the perspective of a non-bank participant. The presentations for the meeting should be available in due course on the webpage of the Group, alongside with the documents from previous meetings. The next regular BMCG meeting is scheduled for 12 October 2016.

Eurosystem: Vision on the future of financial market infrastructure

The Eurosystem's long-term *Vision on the Future of Europe's Financial Market Infrastructure* continues to take shape. A first consultation, focusing on the planned integration of the TARGET2 and TARGET2-Securities platforms, was concluded in April 2016. All responses to this consultation have been published, including a submission from the ICMA ERCC Operations Group, and the ECB is currently reviewing the feedback received. Further details on the other two pillars of the project, instant payments solutions and a potential Common Eurosystem Collateral Management System, are expected to be published in the course of 2016.

The Eurosystem's Future Vision initiative was first outlined in a speech by Yves Mersch (Member of the ECB's Executive Board) given in October 2015, framing the objectives and the scope of the initiative.

In the context of the Eurosystem's Future Vision initiative, the ECB is also planning to hold regular events to encourage collaboration and discussion with market participants. As a vital part of this strategy, the ECB established a new event format, the Focus Session, which builds up on the experience with the previous T2S Info Sessions, but broadens the range of topics discussed beyond T2S and the post-trade world to address current market integration topics more generally. A first Focus Session was held on 8 April 2016, hosted by the Banco de España in Madrid. Besides some general updates on the Eurosystem's Future Vision initiative and on the latest developments in the Spanish and Portuguese markets, the event also featured three panel discussions. A first group of panellists focused on recent collaborative efforts between regulators and the market to achieve further market infrastructure harmonisation in Europe, including the European Commission's European Post-Trade Forum (EPTF) and work undertaken by the ECB's COGESI Group on collateral harmonisation (which are both covered in this market infrastructure update). A second panel then shifted the focus more concretely to the Eurosystem's Future Vision project and the recent first consultation on the integration of TARGET2 and T2S, to assess the potential benefits from this project for market participants. A third panel finally looked further to the future to discuss the potential for Distributed Ledger Technology (DLT) to profoundly change the future post-trade environment. All presentations from the event are available on the ECB website.

ECB: TARGET2-Securities (T2S)

On 22 June 2016, T2S celebrated its first birthday. After a full year of operation, 7 CSDs are now connected to the common settlement platform. The first 4 CSDs who joined T2S in June 2015, were followed in August by Monte Titoli from Italy, and more recently CSDs from Belgium (NBB-SSS) and Portugal (Interbolsa), which both migrated successfully over the Easter break. But the most significant markets are still to come. An important milestone is due to be achieved in September, when 5 further CSDs are scheduled to connect to T2S, among which Euroclear's three ESES CSDs from Belgium, France and the Netherlands. Testing for this third wave is already well advanced, with the final pre-migration phase launched on 1 June. The full T2S migration plan is available on the ECB website.

On the occasion of the first birthday, the ECB published a new edition of its T2S Special Series entitled *One year with T2S – What's Next?*. The latest edition includes contributions from various key figures of the T2S community who share their views on the T2S experience to date and the way ahead for the project and also includes a range of recent statistics on the T2S operations.

The T2S Advisory Group, the main advisory body to the Eurosystem on T2S-related issues, had its latest regular meeting on 5-6 July. No documents are available from this meeting yet.

As mentioned above, the traditional T2S Info Sessions have been replaced by the new and broader Focus Session format. However, T2S has also organized a range of more specific workshops this year on different T2S functionalities. This included workshops on T2S cash forecast and message output optimization in February, T2S settlement optimisation in May, and T2S GUI usability in June.

European Commission: EPTF

The work of the European Post Trade Forum (EPTF), the new post-trade expert group recently established by the European Commission, continues to progress. The Group has met three times so far, most recently on 19 May 2016. At this latest meeting, ICMA

ERCC Chairman Godfried De Vidts was invited to give a presentation on repos and collateral in the post-trade context. This was complemented by an ISLA presentation focusing on securities lending. All documents from the latest and all previous meetings are available on the EPTF website. The next meeting of the group is scheduled for 13 July 2016.

European Securities and Markets Authority (ESMA)

On 31 May 2016, ESMA launched a further consultation in the context of the EU CSD Regulation. The latest consultation focuses on CSD participant default rules and procedures, as ESMA plans to issue Guidelines on this topic specifying the necessary steps for a CSD to follow in case insolvency proceedings are opened with respect to one or more of its participants. Following the deadline of 30 June 2016 for stakeholders to respond to the consultation, ESMA is now reviewing the input received and plans to finalise the Guidelines by 4Q 2016.

Global Legal Entity Identifier System (GLEIS)

The number of Legal Entity Identifiers (LEIs) issued globally continues to steadily increase and has now reached 450,000. A search engine which provides access to all the LEIs issued to date is available on the website of the Global LEI Foundation (GLEIF), the central operating unit for the GLEIS. Alongside the LEI database, the GLEIF website also provides further detailed statistics on the allocation of LEIs around the world.

More information on the GLEIF is also available in the second annual report, which was published on 3 May 2016 and summarises among other things the status of GLEIF operations.

BIS: Committee on Payments and Market Infrastructures (CPMI)

The CPMI jointly with IOSCO continues to monitor the implementation of the 2012 *Principles for Financial Market Infrastructures* (PFMI). The CPMI-IOSCO assessments undertaken in this context are divided into three levels: (i) Level 1 reports which are based on self-assessments by individual jurisdictions on how they have implemented the different Principles set out in the PFMI; (ii) Level 2 reports that analyse the completeness of jurisdictions' implementation measures and their consistency with PFMI; and (iii) Level 3 reports which look at the consistency in the outcomes of such frameworks. While work is ongoing at all three levels, CPMI-IOSCO most recently published the third regular update to the initial Level 1 assessment report. The latest update, published on 28 June 2016, shows that some further progress has been made, with now 19 of the 28 jurisdictions indicating that they have completed their implementation measures for all FMI types.

"The number of Legal Entity Identifiers (LEIs) issued globally continues to steadily increase and has now reached 450,000.

On 29 June 2016, CPMI-IOSCO released their final report, *Guidance on Cyber Resilience for Financial Market Infrastructures.* The final version of the report follows up on an earlier draft which had been published for public consultation in November 2015. The report does not introduce additional standards for FMIs but provides specific clarifications on some of the Principles in the PFMI in relation to cybersecurity concerns. It is the first internationally agreed guidance on this topic for the financial industry.

Distributed Ledger Technology

The potential of Distributed Ledger Technology (DLT) or Blockchain to fundamentally innovate and change the current post-trade environment continues to stir excitement in the industry. Also regulators are getting increasingly involved in this topic. Most recently, on 2 June 2016, ESMA published a Consultation Paper on *Distributed Ledger Technology Applied to Securities Markets.* This follows up on an earlier Call for Evidence on Investment using virtual currency or distributed ledger technology (published in April 2015). Stakeholders have time until 2 September 2016 to submit a response to this consultation.

The ECON Committee of the European Parliament has also finalised its first assessment of DLT. The ECON *Report on Virtual Currencies* was formally adopted in the Committee on 26 April 2016.

Also worth mentioning in this context is a recent paper by the ECB entitled *Distributed Ledger Technologies in Securities Post-trading: Revolution* *or Evolution*; the first detailed analysis of the topic by the ECB.

A more detailed overview of all main recent initiatives by regulators in relation to DLT as well as some other relevant links and sources on this topic are available on a recently launched ICMA resources webpage on DLT.

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Macroprudential risk

On 6 April 2016, the EBA published the periodical update of its Risk Dashboard summarising the main risks and vulnerabilities in the banking sector on the basis of the evolution of a set of risk indicators across the EU in 4Q 2015. The update shows a further increase in EU banks' capital ratios. Profitability remains low and NPL ratios are still high. The figures covered in the Risk Dashboard are based on a sample of 154 banks at the highest level of consolidation, while country aggregates may also include large subsidiaries. The Risk Dashboard is part of the regular risk assessment conducted by the EBA and complements the *Risk Assessment Report*.

On 7 April, the Joint Committee of the ESAs published its, Spring 2016, *Report on Risks and Vulnerabilities in the EU Financial System*, in which three main risks affecting the European financial system are highlighted and a set of policy actions to tackle those risks is suggested:

- The low profitability of financial institutions in a low yield environment poses key concerns to the EU financial system, as financial institutions intend to reduce costs and adjust their business models, forward-looking supervisory approaches to scrutinize business model sustainability are needed; and a proactive stance to address still high stocks of non-performing loans at banks in some regions is also needed.
- Increasing interconnectedness of bank and non-bank entities has arisen over the last five years – with the interconnectedness between different entities representing a potential channel for the propagation of shocks, which needs to be tackled through enhanced supervisory monitoring of concentration risks, cross border exposures and regulatory arbitrage.
- Potential contagion from China and other emerging markets, as their positive contribution to global economic growth, seen over a decade, has started to recede – such that national supervisors now need to include emerging market risk in sensitivity analyses or stress tests and to scrutinise optimistic assumptions of financial institutions with regard to emerging market exposure and returns from emerging market business.

Effective Macroprudential Policy: Cross-Sector Substitution from Price and Quantity Measures is an IMF staff working paper, published on 21 April 2016. As macroprudential policy is increasingly being implemented worldwide, its effectiveness in influencing bank credit and its substitution effects beyond banking have been a key subject of discussion. The authors' empirical analysis confirms the expected effects of macroprudential policies on bank credit, both for advanced and emerging market economies. Yet the authors also find evidence of substitution effects towards non-bank credit, especially in advanced economies, reducing the policies' effect on total credit. Quantity restrictions are particularly potent in constraining bank credit but also cause the strongest substitution effects. Thus, policy implications indicate a need to extend macroprudential policy beyond banking, especially in advanced economies.

“Increasing interconnectedness of bank and non-bank entities has arisen over the last five years – with the interconnectedness between different entities representing a potential channel for the propagation of shocks.

On 25 April, the EBA published the first list of Other Systemically Important Institutions (O-SIIs) in the EU. O-SIIs are those institutions which are deemed systemically relevant in addition to Global Systemically Important Institutions (G-SIIs), already identified. The institutions have been identified by relevant authorities across the EU according to harmonised criteria provided by the EBA. This list reflects also the additional capital buffers that the relevant authorities have set for the O-SIIs they have identified.

On 26-27 April, the first annual ECB Macroprudential Policy and Research Conference, jointly organised with the IMF, was held in Frankfurt. Within the meeting agenda, the ECB has made available links to related documentation. Speeches given during the course of the conference were *The Rationale for Macroprudential Policy*, by Lars Svensson, Stockholm School of Economics; *Principles of Macroprudential Policy*, by Vítor Constâncio, Vice-President of the European Central Bank; and *Macroprudential Policy: Implementation and Effectiveness*, by Donald Kohn, Bank of England and Brookings Institution. During the two days, ten papers were presented and discussed during the course of three sessions: financial cycles, imbalances and early warning indicators; macroprudential regulatory instruments: theory, empirical results and practical experience; and the scope of macroprudential policy, regulatory arbitrage and the role of non-bank activities in systemic risk.

On 7 May, the BIS and the CGFS jointly hosted the third workshop on research on global financial stability. The workshop focused on empirical work related to international banking and financial markets, with emphasis on analysis based in whole or in part on the international banking, debt securities and derivatives statistics compiled by the BIS on behalf of the CGFS. The workshop was intended to promote the use of these statistics, including the newly enhanced banking statistics, among central bankers, analysts and academics.

On 11 May, ESMA published its Risk Dashboard for 1Q 2016, which shows that the overall risks to securities markets in Q1 2016 remained unchanged at high levels, with market and credit risks being very high. This was reflected in major price swings in global equity markets, especially affecting financial institutions at the beginning of 1Q 2016, and high volatilities across market segments. Corporate bond spreads increased substantially, especially for lower rated bonds, before moderating at the end of 1Q 2016. Key risk sources were mostly related to the uncertain EU and global economic outlook, commodities price dynamics and global financial developments. Liquidity risk was at high levels amid sustained investors' uncertainty, potentially leading to portfolio reallocation and related liquidity pressures. Contagion risk was also high, the main drivers including financial market interconnectedness related to the exposure of EU financial and non-financial sectors to EM and the commodities sector, as well as increased interconnectedness of the fund sector with the rest of the financial system. Systemic stress increased during the first part of the first quarter before easing in March 2016, mainly driven by bond and equity market dynamics.

On 13 May, the ESRB published *A Review of Macroprudential Policy in the EU in 2015*. In brief, the Executive Summary reports that:

- compared to the previous year, 2015 saw a substantial increase in the number of macroprudential measures in the EU;
- some Member States opted for an early introduction of the countercyclical capital buffer in 2015;
- most Member States identified the G-SIIs and O-SIIs in their jurisdiction and set additional capital buffer requirements; and
- the real estate sector remains a key priority for many macroprudential authorities.

On 24 May, the ECB published its latest semi-annual *Financial Stability Review*. According to this Review: (i) Europe's financial system showed resilience in face of rising vulnerabilities stemming from emerging market economies and financial market turbulence over the past six months; (ii) economic and financial vulnerabilities persist in the form of high legacy debt, both public and private, and a weak economic recovery; and (iii) euro area banking sector repair continues amid challenges to profitability and, in some countries, high stocks of non-performing loans. But risks extend also to the real economy. In particular, concerns remain about euro area sovereign debt sustainability despite relatively benign financial market conditions. Political risks have increased considerably in almost all euro area countries in recent years; whilst higher political uncertainty may further delay structural reforms and possibly exert renewed pressure on more vulnerable sovereigns. There are also risks that stem from outside the traditional banking sector, including that over the past few years assets managed by investment funds have expanded rapidly at the same time as such funds have gradually increased their exposure to the riskier segments of the financial markets.

The ECB has singled out four systemic risks to financial stability over the next two years: (i) further increase of risk premia and financial turmoil, triggered by emerging market stress and persistently low commodity prices; (ii) weak profitability prospects for banks and insurers, with banks' intermediation additionally constrained by unresolved problems in reducing non-performing loans; (iii) rising debt sustainability concerns in sovereign and non-financial private sectors amid heightened political uncertainty and low nominal growth; and (iv) prospective stress in the investment fund sector amplified by liquidity risks and spillovers to the broader financial system. Finally, the Review also contains three special features: (i) the general case for setting macroprudential margins and haircuts on derivatives and SFTs; (ii) examination of the systemic implications of the bail-in tool under the BRRD; and (iii) a review of recent trends in business model characteristics, with discussion of how they affect bank stability and performance.

Under date of 16 June, the European Parliament published two briefing papers. The first of these looks back at five years of existence of the ESRB and gives an overview of its concrete output; and the second provides an overview of the EU macroprudential policy framework in its various components and also provides some examples of national macroprudential measures taken to date.

On 21 June, Mario Draghi, in his capacity as Chair of the ESRB, spoke at a hearing before the Committee on Economic and Monetary Affairs (ECON) of the European Parliament. Commenting firstly on the medium-term impact of the low level of interest rates from a macroprudential angle, Mario Draghi flagged that the financial stability risks related to low interest rates could materialise in different parts of the financial system. The ESRB therefore needs to take a holistic view when designing policy responses. To this end, they are looking at three main groups of risks: (i) the sustainability of business models, (ii) broad-based risk-taking, and (iii) changes in the structure of the financial system.

Looking ahead, Mario Draghi then highlighted another topic important to the ESRB, namely developing a strategy for macroprudential policy beyond the banking sector – a task which will require a broad range of stakeholders in Europe to work together, including legislators, the ESRB, macro- and microprudential authorities and conduct regulators. What is needed is an analytical and policy framework to target risks across the whole financial system with a consistent, albeit not necessarily uniform, set of instruments, including those for insurance, financial markets and market infrastructure. The ESRB are proposing to develop a wider financial stability toolkit, including top-down stress tests for asset managers, CCPs, insurers and pension funds as well as recovery and resolution frameworks for CCPs and insurers; and will soon be publishing a strategy paper on this.

Mario Draghi next spoke about liquidity, commenting on the ESRB's work on assessing risks to the investment fund and market-making sectors in Europe. The ESRB's first technical assessment based on macro-stress calculations leads to the conclusion that 95% of the asset management firms and investment funds in their sizeable sample would be able to fully satisfy redemption claims in an "extreme but plausible" scenario. As regards the recent regulatory changes and their potential unintended impact on market liquidity, Mario Draghi stated that it is important to remember the intended aims of the new rules: stricter regulation means market-makers are better able to absorb losses under stressed market conditions, thereby increasing market resilience and reducing the risk of market disruptions in times of stress. Finally, Mario Draghi also commented on some recent ESRB publications.

The General Board of the ESRB held its 22nd regular meeting, on 23 June. The risk of repricing in financial markets and the further weakening of financial institutions' balance sheets were highlighted by the General Board as the main risk to financial stability in the EU. The General Board also discussed key conditions that contribute to increasing vulnerability in the EU banking sector – namely: low profitability in an environment of low interest rates; the burden of non-performing legacy assets, which is particularly high in some EU countries; and the excess supply of services provided by banks. The General Board emphasised that addressing these challenges should remain a top priority for EU policymakers. The General Board continues to discuss macroprudential issues and structural changes related to the low interest rate environment, with a view to identifying areas in which macroprudential policies may be needed.

The financial stability implications of the possible imbalances between the demand for and supply of market liquidity are an important macroprudential issue, as these imbalances could amplify and/or transmit shocks through the financial system. Against this background, the ESRB has assessed risks for investment funds and market-makers in Europe. This work benefited from the ESRB's ability to gather data and conduct analyses across all EU Member States. The General Board endorsed the publication of the ESRB report, which discusses the results of the ESRB's assessment as regards the market-making sector (this document will be published this summer).

Moreover, the General Board endorsed the publication of the ESRB's strategy paper on macroprudential policy beyond banking. While macroprudential policy for the banking sector is

The financial stability implications of the possible imbalances between the demand for and supply of market liquidity are an important macroprudential issue, as these imbalances could amplify and/or transmit shocks.

already operational, the policy strategy, regulatory data and instruments required to address risks beyond the banking sector need further enhancement. The ESRB paper therefore analyses the current legal and institutional framework governing macroprudential policies beyond banking and proposes a holistic policy strategy to address financial stability risks (this paper will be published in July).

On 21 June, EIOPA published its June 2016 report on financial stability in the (re)insurance and occupational pension fund sectors of the EEA. EIOPA observes an ongoing extremely challenging macro-economic and financial environment. Monetary policy and low crude oil prices imply a protracted low yield environment in the short- to medium-term. In this environment, the "double-hit" scenario, of a negative market shock to asset prices combined with a low risk free rate, cannot be ruled out. Both risks (low yields and a double-hit) will be in the focus of EIOPA's Insurance Stress Test 2016.

On 26 June, Hyun Song Shin, Economic Adviser and Head of Research, gave a presentation, *Liquidity, Leverage and Macro Risk*, on the occasion of the BIS AGM. The realignment of the global economy has been most evident in the large adjustments of exchange rates. The BIS Annual Report examines how these exchange rate adjustments have been both a symptom of and a catalyst for recent events. Apparently disparate issues, such as market liquidity, currency market anomalies and the risk-taking capacity of financial intermediaries, can be understood better by reference to a few common themes, especially the role of accumulated stocks in accentuating the impact of shocks. BIS findings reinforce the macroeconomic rationale for prudential policy – as a better capitalised financial sector is conducive not only to greater resilience of the financial system, but also to greater risk-taking capacity in support of more liquid financial markets and better macro outcomes.

On 30 June, the ESRB released Issue 16 of its Risk Dashboard, which is a set of quantitative and qualitative indicators of systemic risk in the EU financial system. In summary, the published overview indicates that (i) systemic risk as perceived by markets decreased at the end of the first quarter of 2016, following an increase at the beginning of the year; (ii) economic recovery in the EU continues; but levels of debt continue to remain a source of vulnerability in several countries, both for the public and the non-financial corporate sectors; (iii) bank lending to both households and the non-financial corporate sector continued its gradual recovery; yet the picture for lending standards is mixed; (iv) banks' profits decreased for the third consecutive quarter, as measured by the average return on equity; and (v) as in the previous quarter, the size of the non-banking and non-insurance segments of the financial sector continued to grow in the fourth quarter.

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ICMA Capital Market Research

Remaking the Corporate Bond Market: ICMA's 2nd Study into the State and Evolution of the European Investment Grade Corporate Bond Secondary Market

Published: 6 July 2016
Author: Andy Hill, ICMA

Evolutionary Change: The future of electronic trading in European cash bonds

Published: 20 April 2016
Author: Elizabeth Callaghan, ICMA

Perspectives from the Eye of the Storm: The Current State and Future Evolution of the European Repo Market

Published: 18 November 2015
Author: Andy Hill, ICMA

Impact Study for CSDR Mandatory Buy-ins

Published: 24 February 2015
Author: Andy Hill, ICMA

The Current State and Future Evolution of the European Investment Grade Corporate Bond Secondary Market: Perspectives from the Market

Published: 25 November 2014
Author: Andy Hill, ICMA

Continually Working to Develop Efficient and Effective Collateral Markets

ERC Occasional Paper

Published: 4 September 2014
Author: David Hiscock, ICMA

Covered Bond Pool Transparency: the Next Stage for Investors

Published: 21 August 2014
Author: Prepared for ICMA by Richard Kemmish Consulting Ltd

Collateral is the New Cash: The Systemic Risks of Inhibiting Collateral Fluidity

Published: 3 April 2014
Author: Andy Hill, ICMA

Avoiding Counterproductive Regulation in Capital Markets: A Reality Check

Published: 29 October 2013
Author: Timothy Baker, Senior Adviser to ICMA

Collateral Damage: the Impact of the Financial Transaction Tax on the European Repo Market and its Consequences for the Financial Markets and the Real Economy

Published: 8 April 2013
Author: Richard Comotto, ICMA Centre

Economic Importance of the Corporate Bond Markets

Published: 8 April 2013
Author: Timothy Baker, Senior Adviser to ICMA

ICMA Events and Education

ICMA Annual General Meeting and Conference

Dublin May 18 to 20, 2016

ICMA's 48th AGM and Conference in Dublin at the end of May attracted a record turnout of close to 1,000 delegates in total. The varied panels and speakers, focused on ICMA's priority areas of primary markets, secondary markets, repo and collateral, green finance and sustainability, and our buy-side work. At the AGM itself six new Board members joined an expanded ICMA board reflecting ICMA's increasingly diversified reach in international markets. ICMA members voted to allow recognised trading venues, CCPs and clearing and settlement entities to become full rather than associate members in recognition of their increasingly critical role in the debt securities markets. Next year's AGM and conference will take place in Stockholm.

ICMA Women's Network - events past and future.

The ICMA Women's Network rolled out events for ICMA members across Europe in the spring.

In April, French members gathered for the launch event of the France Committee of the ICMA Women's Network: *Are Women Not Putting Themselves Forward as Candidates: Myth or Reality?* The event focused on practical tips for getting yourself and your ideas noticed at work and for making a positive impact when interacting with colleagues and clients, all in the context of career development in financial services.

The conference started with a panel discussion with senior industry figures who share their own experiences and successful strategies that helped them to progress their careers. This debate was followed by a presentation on "the superiority of women in reading non-verbal communication and how to transform those intuitions into certainties" delivered by Marwan Mery, Co-Founder of ADN Group, Professional Negotiator and Expert in Lie Detection. Speed mentoring sessions and a networking reception rounded off the evening.

In Zurich in June, the ICMA Women's Network (IWN) in Switzerland held its first event, *Starting Out*, where a panel of inspirational industry figures discussed where their careers in financial services began, the challenges they faced as they progressed and the advice they would offer their younger selves. The event, which was kindly hosted by UBS, was followed by drinks and focused networking.

And in London, the IWN summer event, *Bouncing Back – Developing Resilience at Work*, was hosted jointly with ICMA members Lloyds Bank Capital Markets at the Barbican Atrium on 15 June. Our largest ever audience for an IWN event heard professional resilience coach, psychologist and author Jane Clarke of Nicholson McBride explain the importance of resilience in a professional context, how it can help you to handle difficult situations and setbacks and, most importantly, how to develop resilience. Having identified the five key elements of resilience in a work context, Jane went on to give some useful practical techniques for improving individual performance in all of them. For example, reframing beliefs to go from "why does this always happen to me?" to "this happens to everyone – I can sort it out" was cited as one powerful way to develop solution orientation when problems arise. Delegates joined us for drinks and animated discussions of the details of the presentation in the beautiful Barbican Conservatory.

Save the date for the IWN Winter Event with Julia Hoggett of the FCA on 22 November 2016.

Contact: ICMAwomensnetwork@icmagroup.org

diary

Workshops

13 SEP

Ethics and the Capital Markets, Frankfurt, 13 September

Are we in danger of relying too much on a compliance-driven culture to protect the financial markets, rather than re-establishing a clear ethical culture – both at the individual and the corporate level? This new ICMA Workshop seeks to redress the balance and raise awareness of ethics and bringing ethical values to bear in the financial markets.

Register

20-22 SEP

Repo and Securities Lending under the GMRA and GMSLA, London, 20-22 September

The workshop analyses how repo and securities lending transactions operate within the framework provided by the Global Master Repurchase Agreement (GMRA) and the Global Master Securities Lending Agreement (GMSLA), and highlights the issues that need to be addressed by users.

Register

18 OCT

European Regulation: An Introduction for Capital Market Practitioners, London, 18 October

How much do you know about the new regulations that are already in force and impacting your daily work in the capital market and the ones that are still in the pipeline? Against a background of far-reaching regulatory change ICMA's one-day, fast-track course on European regulation for capital market practitioners gives an overview of the new regulatory landscape for financial institutions in Europe.

Register

27 OCT

Bond Syndication Practices for Compliance Professionals and Other Non-Bankers, London, 27 October

This workshop aims to give compliance professionals an in-depth and thorough understanding of the current practices that are involved in launching a deal in the international debt capital market.

Register

Seminars & Conferences

ICMA organises over 100 market-related events each year attended by members and non-members.

Save the date for these ICMA events in autumn/winter 2016

ICMA European Repo and Collateral Council (ERCC) General Meeting, London, 27 September

ICMA Asset Management and Investors Council (AMIC) Conference, London, 7 November

ICMA Conference: An update on the Green Bond Principles, Zurich, 16 November

ICMA Capital Market Lecture Series: Jean-Claude Trichet, London, 7 December

29 SEP

The 8th Annual bwf and ICMA Capital Markets Conference, Frankfurt, 29 September

The 8th Annual bwf and ICMA Capital Markets Conference will take place at the Deutsche Nationalbibliothek (German National Library). It will again take a look at the current issues facing capital market participants with specific emphasis on the German perspective.

Register

23 NOV

The 10th ICMA Primary Market Forum, London, 23 November

Now in its 10th year, the ICMA Primary Market Forum will bring together issuers, syndicate banks, investors and law firms active in primary debt capital markets to discuss the developments and the outlook for the future.

Register

For full details see icmagroup.org

ICMA Executive Education

Courses in 2016

Level I: Introductory Qualifications

Financial Markets Foundation Course (FMFC)
Luxembourg: **21-23 September 2016**
London: **2-4 November 2016**

Financial Markets Foundation Course (FMFC) Online Programme

Next start date: **1 August** (register by 26 July 2016)

Introduction to Fixed Income (IFI)

London: **19-21 October 2016**

Introduction to Primary Markets (IPM)

London: **24-26 October 2016**

Securities Operations Foundation Course (SOFC)

London: **28-30 September 2016**
Brussels: **9-11 November 2016**

Securities Operations Foundation Course (SOFC) Online Programme

Next start date: **1 August** (register by 26 July 2016)

Level II: Intermediate Qualifications

Fixed Income Certificate (FIC)

Barcelona: **24-28 October 2016**

Fixed Income Certificate (FIC) Online Programme

Next start date: **1 October 2016**
(register by 27 September 2016)

Operations Certificate Programme (OCP)

Brussels: **14-18 November 2016**

Primary Market Certificate (PMC)

London: **21-25 November 2016**

Level III: Specialist Training Programmes

Fixed Income Portfolio Management

London: **26-27 September 2016**

Corporate Actions - An Introduction

London: **10-11 October 2016**

Corporate Actions - Operational Challenges

London: **12-13 October 2016**

Collateral Management

London: **17-18 October 2016**

ICMA Guide to Best Practice in the European Repo Market

London: **31 October 2016**

Trading & Hedging Short-term Interest Rate Risk

London: **8-9 November 2016**

Trading the Yield Curve with Interest Rate Derivatives

London: **10-11 November 2016**

Inflation-linked Bonds & Structures

London: **29-30 November 2016**

Credit Default Swaps – Pricing, Application & Features

London: **5-6 December 2016**

Credit Default Swaps – Operations

London: **7 December 2016**

For more information contact: education@icmagroup.org or visit www.icmagroup.org/education

GLOSSARY

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ABCP	Asset-Backed Commercial Paper
ABS	Asset-Backed Securities
ADB	Asian Development Bank
AFME	Association for Financial Markets in Europe
AIFMD	Alternative Investment Fund Managers Directive
AMF	Autorité des marchés financiers
AMIC Council	ICMA Asset Management and Investors Council
ASEAN	Association of Southeast Asian Nations
ASF	Available Stable Funding
AuM	Assets under management
BBA	British Bankers' Association
BCBS	Basel Committee on Banking Supervision
BIS	Bank for International Settlements
BMCG	ECB Bond Market Contact Group
BRRD	Bank Recovery and Resolution Directive
CAC	Collective action clause
CBIC	ICMA Covered Bond Investor Council
CCBM2	Collateral Central Bank Management
CCP	Central counterparty
CDS	Credit default swap
CFTC	US Commodity Futures Trading Commission
CGFS	Committee on the Global Financial System
CICF	Collateral Initiatives Coordination Forum
CIF	ICMA Corporate Issuer Forum
CMU	Capital Markets Union
CNAV	Constant net asset value
CoCo	Contingent convertible
COGESI	Contact Group on Euro Securities Infrastructures
COP21	Paris Climate Conference
COREPER	Committee of Permanent Representatives (in the EU)
CPMI	Committee on Payments and Market Infrastructures
CPSS	Committee on Payments and Settlement Systems
CRA	Credit Rating Agency
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CSD	Central Securities Depository
CSDR	Central Securities Depositories Regulation
DLT	Distributed Ledger Technology
DMO	Debt Management Office
D-SIBs	Domestic systemically important banks
DVP	Delivery-versus-payment
EACH	European Association of CCP Clearing Houses
EBA	European Banking Authority
EBRD	European Bank for Reconstruction and Redevelopment
ECB	European Central Bank
ECJ	European Court of Justice
ECOFIN	Economic and Financial Affairs Council (of the EU)
ECON	Economic and Monetary Affairs Committee of the European Parliament
ECP	Euro Commercial Paper
ECPC	ICMA Euro Commercial Paper Committee
EDGAR	US Electronic Data Gathering, Analysis and Retrieval
EEA	European Economic Area
EFAMA	European Fund and Asset Management Association
EFC	Economic and Financial Committee (of the EU)
EFSF	European Financial Stability Facility
EFSI	European Fund for Strategic Investment
EFTA	European Free Trade Area
EGMI	European Group on Market Infrastructures
EIB	European Investment Bank
EIOPA	European Insurance and Occupational Pensions Authority
ELTIFs	European Long-Term Investment Funds
EMDE	Emerging market and developing economies
EMIR	European Market Infrastructure Regulation
EMTN	Euro Medium-Term Note
EMU	Economic and Monetary Union
EP	European Parliament
ERCC	ICMA European Repo and Collateral Council
ESA	European Supervisory Authority
ESFS	European System of Financial Supervision
ESMA	European Securities and Markets Authority
ESM	European Stability Mechanism
ESRB	European Systemic Risk Board
ETF	Exchange-traded fund
ETP	Electronic trading platform
ESG	Environmental, social and governance
ETD	Exchange-traded derivatives
EURIBOR	Euro Interbank Offered Rate
Eurosystem	ECB and participating national central banks in the euro area
FAQ	Frequently Asked Question
FASB	Financial Accounting Standards Board
FATCA	US Foreign Account Tax Compliance Act
FATF	Financial Action Task Force
FCA	UK Financial Conduct Authority
FEMR	Fair and Effective Markets Review
FICC	Fixed income, currency and commodity markets
FIIF	ICMA Financial Institution Issuer Forum
FMI	Financial market infrastructure
FMSB	FICC Market Standards Board
FPC	UK Financial Policy Committee
FRN	Floating-rate note
FSB	Financial Stability Board
FSC	Financial Services Committee (of the EU)
FSOC	Financial Stability Oversight Council (of the US)
FTT	Financial Transaction Tax
G20	Group of Twenty
GBP	Green Bond Principles
GDP	Gross Domestic Product
GMRA	Global Master Repurchase Agreement
G-SIBs	Global systemically important banks
G-SIFIs	Global systemically important financial institutions
G-SIIs	Global systemically important insurers
HFT	High frequency trading
HMRC	HM Revenue and Customs
HMT	HM Treasury
IAIS	International Association of Insurance Supervisors
IASB	International Accounting Standards Board
ICMA	International Capital Market Association
ICSA	International Council of Securities Associations
ICSDs	International Central Securities Depositaries
IFRS	International Financial Reporting Standards
IG	Investment grade
IIF	Institute of International Finance
IMMFA	International Money Market Funds Association
IMF	International Monetary Fund
IMFC	International Monetary and Financial Committee
IOSCO	International Organization of Securities Commissions
IRS	Interest rate swap
ISDA	International Swaps and Derivatives Association
ISLA	International Securities Lending Association
ITS	Implementing Technical Standards
KfW	Kreditanstalt für Wiederaufbau
KID	Key information document
KPI	Key performance indicator
LCR	Liquidity Coverage Ratio (or Requirement)
L&DC	ICMA Legal & Documentation Committee
LEI	Legal entity identifier
LIBOR	London Interbank Offered Rate
LTRO	Longer-Term Refinancing Operation
MAD	Market Abuse Directive
MAR	Market Abuse Regulation
MDB	Multilateral Development Bank
MEP	Member of the European Parliament
MiFID	Markets in Financial Instruments Directive
MiFID II	Revision of MiFID (including MiFIR)
MiFIR	Markets in Financial Instruments Regulation
MMCG	ECB Money Market Contact Group
MMF	Money market fund
MOU	Memorandum of Understanding
MREL	Minimum requirement for own funds and eligible liabilities
MTF	Multilateral Trading Facility
NAFMII	National Association of Financial Market Institutional Investors
NAV	Net asset value
NCA	National competent authority
NCB	National central bank
NSFR	Net Stable Funding Ratio (or Requirement)
OAM	Officially Appointed Mechanism
OJ	Official Journal of the European Union
OMTs	Outright Monetary Transactions
ORB	London Stock Exchange Order book for Retail Bonds
OTC	Over-the-counter
OTF	Organised Trading Facility
PCS	Prime Collateralised Securities
PD	Prospectus Directive
PD II	Amended Prospectus Directive
PMPC	ICMA Primary Market Practices Committee
PRA	UK Prudential Regulation Authority
PRIIPs	Packaged Retail and Insurance-Based Investment Products
PSE	Public Sector Entities
PSI	Private Sector Involvement
PSIF	Public Sector Issuer Forum
QE	Quantitative easing
QIS	Quantitative impact study
QMV	Qualified majority voting
RFQ	Request for quote
RM	Regulated Market
RMB	Chinese renminbi
ROC	Regulatory Oversight Committee of the Global Legal Entity Identifier System
RPC	ICMA Regulatory Policy Committee
RSF	Required Stable Funding
RSP	Retail structured products
RTS	Regulatory Technical Standards
RWA	Risk-weighted assets
SEC	US Securities and Exchange Commission
SFT	Securities financing transaction
SGP	Stability and Growth Pact
SI	Systematic Internaliser
SLL	Securities Law Legislation
SMEs	Small and medium-sized enterprises
SMPC	ICMA Secondary Market Practices Committee
SMSG	Securities and Markets Stakeholder Group (of ESMA)
SPV	Special purpose vehicle
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SRO	Self-regulatory organisation
SSAs	Sovereigns, supranationals and agencies
SSM	Single Supervisory Mechanism
SSR	EU Short Selling Regulation
STORs	Suspicious transactions and order reports
STS	Simple, transparent and standardised
T+2	Trade date plus two business days
T2S	TARGET2-Securities
TD	EU Transparency Directive
TFEU	Treaty on the Functioning of the European Union
TLAC	Total Loss-Absorbing Capacity
TMA	Trade matching and affirmation
TRs	Trade repositories
UKLA	UK Listing Authority
VNAV	Variable net asset value

ICMA welcomes feedback and comments on the issues raised in the Quarterly Report. Please e-mail: regulatorypolicynews@icmagroup.org or alternatively the ICMA contact whose e-mail address is given at the end of the relevant article.

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