ICMA
International Capital Market Association

QUARTERLY REPORT

ASSESSMENT OF MARKET PRACTICE AND REGULATORY POLICY

INSIDE:

PROGRESS IN TRANSITIONING TO RISK-FREE RATES

OPPORTUNITIES FOR DEEPENING CAPITAL MARKETS UNION

INITIATIVES ON SUSTAINABLE FINANCE

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ICMA
International Capital Market Association

The mission of ICMA is to promote resilient and well-functioning international and globally integrated cross-border debt securities markets, which are essential to fund sustainable economic growth and development.

ICMA is a membership association, headquartered in Switzerland, committed to serving the needs of its wide range of members. These include public and private sector issuers, financial intermediaries, asset managers and other investors, capital market infrastructure providers, central banks, law firms and others worldwide. ICMA currently has over 580 members located in 62 countries.

ICMA brings together members from all segments of the wholesale and retail debt securities markets, through regional and sectoral member committees, and focuses on a comprehensive range of market practice and regulatory issues which impact all aspects of international market functioning. ICMA prioritises four core areas – primary markets, secondary markets, repo and collateral markets, and the green and social bond markets.

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Reflections on an exceptionally busy year for ICMA

By Martin Scheck

Let me start by thanking all of you for your support last year, through your membership, active participation on our committees and councils, and support of our many events. I would also like to thank specifically the ICMA Board for their time, support and guidance over the year, and our dedicated and experienced staff for all their efforts and continual sheer hard work.

ICMA's resources are deployed in four major areas: the primary markets, secondary markets, repo and collateral and sustainability. In each area, we focus on the market as a whole, involving the sell side and the buy side together. We also focus on the impact of new financial technology across these areas and on helping avoid unnecessary market fragmentation.

Last year there were four overriding themes – sustainability, the transition from IBORs to risk-free rates, Brexit and continuing market access, and FinTech. All will affect the way our members do business in the capital market, and so our engagement on their behalf is necessarily extensive.

Sustainability emerged at or near the top of the agenda for the public and politicians in most countries last year, with increasing demand for private sector financing for the changes we need to make. Whilst we continue to oversee the evolution of the Green and Social Bond Principles through our work as the secretariat for the growing GBP/SBP community, ICMA's overall engagement now runs even deeper. We are a member of the European Commission's Technical Expert Group and have been involved in the development of both the new European taxonomy and the EU green bond standard. ESG disclosure is an increasingly important topic for our buy-side members and also for our issuer community. We are committed to playing a full role in the globally coordinated development of green and social finance, working on definitions and market practice in many different jurisdictions with members and the authorities - China, ASEAN, Japan, Russia, India, and the US as well as Europe, promoting the sector at events across the world and offering education courses.

As far as the transition to risk-free rates is concerned, we are directly involved in the risk-free rate working groups of the UK, the euro area and Switzerland and have regular calls with the ARRC in the US. Our focus is on the bond markets, where we continue to chair the sterling bond market transition group, working with the FCA and the Bank of England. The transition from the IBORs to risk-free rates is complex and far-reaching and, whilst adoption of the new risk-free rates in the bond market is going well in many jurisdictions (and extremely well in the GBP market), the legacy problem is not yet solved. We have commented on the transition widely in the Quarterly Report, through a series of member calls in Europe and Asia and in many committee meetings and individual member discussions. This will continue to be a dominant theme for at least the next two years.

In December, the UK held a general election which has clarified the UK's position on Brexit. ICMA is not of course involved in politics. Our focus has been on the potential market impact of Brexit, where we have updated our members regularly on the situation as it emerges, both as regards the market impact of so-called cliff-edge risks when passporting rights between the EU27 and the UK cease, and the scope for regulatory equivalence after Brexit. It would appear that most of our major buy and sell-side members are now set up and authorised so as to be able to serve clients in both the EU27 and the UK, but nevertheless smaller members may not yet be ready. We will continue our work on Brexit as long as necessary.

In the fast-changing domain of FinTech, which is rapidly reshaping our market, we have chosen initially to help our members by providing information on what solutions are commercially available to them - through our mapping directories in the primary and secondary markets and in repo operations and by promoting information exchange between FinTech providers and members at meetings and conferences. We have also built relationships with a broader set of relevant regulators and are keenly monitoring international developments in this area. A newly established FinTech committee of members will help guide our future efforts.

Aside from these major themes, the important day-to-day work with our members continues. For example, the advocacy and education around the impact of the mandatory buy-in regime under CSDR has been augmented with a new impact study. The study predicted a rather negative effect on liquidity, in particular for lower credit quality bonds. This is a complex topic and we are working with ESMA and the Commission to explain our perspective and look for ways to mitigate the harmful impact of mandatory buy-ins.

The repo market has always been a vital – though not always fully appreciated – part of the financial markets. It has reached greater prominence this year. The forthcoming SFT Regulation due to be implemented in early 2020 is a major challenge for market participants, given the scale and complexity of the reporting requirements embodied in the Regulation, whose impact will be felt in markets far beyond the borders of Europe. ICMA has been leading the industry response to standardising and clarifying the reporting requirements - the volume of information for each trade is immense and most fields need to match exactly in order to settle – and hence the industry effort to harmonise the reporting is essential.

Our expertise on repo is in demand from many areas outside Europe, and we have been happy to share this with members and regulators, holding repo seminars and courses all over the world. As an example, we work with FrontClear in sub-Saharan Africa to promote capacity building and also with the authorities in the Philippines and in Indonesia. Repo market developments are also under way in China and ICMA has been happy to share its expertise and experience in creating international standards and documentation.

Our work continues, two years after MiFID II/R implementation, around MiFID II/R data - where we are providing a useful forum for our members and speaking with the appropriate regulators about how improvements can be achieved. In addition, we are proponents of an EU consolidated tape for non-equities and have been asked by the European Commission to present our views on the rationale, structure and governance of such a data source. Working with a cross-industry group of our members we submitted an interim report in mid-December and are looking forward to continuing our discussions in 2020.

Away from our market practice and regulatory agenda, we have continued to build our outreach to members through the ICMA Women's Network and the ICMA Future Leaders Group. Both have extended their membership again this year, with an extensive schedule of meetings across European finance centres. Our mentoring platform, which allows more junior fixed income professionals to connect with a mentor, has seen a corresponding uptick and the metrics from our social media accounts also show that more of you are choosing to interact with us through them.

In Asia-Pacific, the fastest growing of our regions, we welcomed to ICMA a number of significant new members at different levels of membership ranging from Tier 1 to Tier 3. Our market-leading work on primary markets and sustainability, and the efforts of our team in the Hong Kong office, has resulted in a high profile for ICMA with members and regulators in the region. Last year through outreach in various forms we were able to assist members in better understanding the extra-territorial impact of forthcoming EU regulation. In China we have helped to promote internationalisation of the China Interbank Bond Market, and the growth of the Panda Bond Market.

Executive education remains important to ICMA and our members. 2019 saw continued growth in in-house courses - run in over 11 countries - and the classroom courses performing above 2018 levels against a challenging financial backdrop. The offering is already extensive and in 2020 we will be revamping the online self-study versions of our introductory courses. Full details of all courses are on our website.

Lastly, a quick word on major forthcoming events. ICMA's AGM and Conference is a highlight, running from 24 to 26 June in Vienna, and not to be missed. Similarly, the GBP/SBP AGM and Conference, which last year took place in Frankfurt, is this year planned for New York.

Operationally ICMA is in a good position, financially viable, engaged and with expert staff with a high level of continuity, and with a growing membership - now at a two-decade high.

In this brief summary I have just set out some of the highlights of 2019, but I hope this gives you a good feel for the breadth and depth of our activities. Of course there is much more detail in this Quarterly Report and on the ICMA website.

As ever huge challenges lie ahead, but there is much that can be achieved by working together. Again, many thanks for your support - I wish you all a good new year and look forward to working with you all in 2020.

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The transition from LIBOR to risk-free rates: legacy bonds *By Paul Richards*

Summary

RFR

As part of ICMA's programme to raise awareness of the transition to risk-free rates, this Quarterly Assessment provides a market perspective on the transition of legacy LIBOR bonds, particularly bonds denominated in sterling under English law, and on the continuing need for international coordination.

Introduction

1 Since Andrew Bailey, the Chief Executive of the FCA[1] (the regulator of LIBOR), announced in July 2017 that the FCA would no longer intend to persuade or compel banks to submit contributions for LIBOR after the end of 2021, considerable progress has been made in transitioning from LIBOR to near risk-free rates[2] in the bond market, in particular in the UK through the adoption of SONIA in new bond issues. In 2019, there were 33 different issuers – mainly banks, building societies and SSAs – of new floating rate notes (FRNs) referencing SONIA with a value of over £35 billion; and securitisations referencing SONIA with a value of over £15 billion were distributed to investors.[3] These transactions all used the same market conventions: overnight SONIA compounded over the interest period, with the margin added, and with a five-day lag before the end of each interest period.

2 But challenges remain. The biggest challenge in the bond market is how to transition legacy bonds referencing LIBOR to risk-free rates. Andrew Bailey spoke about this in New York on 15 July 2019:

- "Market participants will ask whether legislation could help. For example, could legislators redefine LIBOR as risk-free rates plus fixed spreads for those tough legacy contracts? Or could they create safe harbours for those adopting consensus industry solutions which enjoy authorities' support such as compounded risk-free rates and fixed spreads? These measures are not in the gift of regulators, but it is sensible to consider their pros and cons."
- He also said: "One task for the second half of this year will be to see if and where consensus exists, so relevant authorities can share and consider the feasibility and consequences of each path. But I want to be very clear – none of the options except that of cessation can be relied upon to be deliverable. Those who can transition should do so."[4]

LIBOR fallbacks

3 Following the adoption of SONIA as the preferred risk-free rate for sterling, new issues of sterling FRNs and securitisations are nearly all now referencing SONIA rather than LIBOR. Consequently, there is no longer a need for fallbacks from sterling LIBOR to SONIA in new bond market documentation. But fallbacks already used in legacy bond contracts referencing sterling LIBOR complicate the transition to risk-free rates in the bond market, as many will fall back to a fixed rate (ie the last available LIBOR fix) when LIBOR is permanently discontinued.[5] These fallback clauses are of three main types:

1. Andrew Bailey has been appointed as the next Governor of the Bank of England with effect from 16 March 2020.

2. In all the main jurisdictions, the chosen risk-free rates are overnight rates: ie SONIA in the UK; SOFR in the US; €STR in the euro area; SARON in Switzerland; and TONA in Japan. A common objective is to make risk-free rates as robust as possible, with robustness measured primarily by the volume of underlying observable transactions.

3. Source: FSB, 18 December 2019. The FSB also reports that over $300 billion in SOFR debt has been issued in the US.

4. Andrew Bailey: *LIBOR: Preparing for the End,* New York, 15 July 2019.

5. This may also be the case with legacy FRNs denominated in other LIBOR currencies, including US dollars.

- *Type 1:* Before Andrew Bailey's speech in July 2017 announcing the potential discontinuation of LIBOR after the end of 2021, most FRNs referencing sterling LIBOR include fallbacks which do not contemplate the permanent discontinuation of LIBOR and rely on the application of the last available LIBOR rate. When LIBOR is permanently discontinued, such fallbacks will result in the rate being fixed for the remaining life of the bond. Some legacy bonds may have fallback language which is unclear or have no fallback provisions at all.[6]
- *Type 2:* Since July 2017, many FRN fallback clauses referencing sterling LIBOR have been drafted to take account of the permanent discontinuation of LIBOR and provide for the application of a successor or alternative rate.
- *Type 3:* Some more recent FRN fallback clauses referencing sterling LIBOR also take account of a possible future declaration by the FCA that LIBOR is no longer representative of its underlying market and so apply on the basis of this "pre-cessation" trigger.[7]

4 Type 1 fallback clauses, which will fall back to a fixed rate (ie the last LIBOR fix) when LIBOR is permanently discontinued, represent much the largest proportion of outstanding legacy sterling LIBOR bond contracts.

The legacy bond problem

5 The adoption of SONIA instead of LIBOR in new bond issues helps to cap the scale of the legacy sterling LIBOR bond problem but does not solve it. Market estimates indicate that legacy bonds referencing LIBOR with a value of at least $864 billion equivalent globally are due to mature beyond the end of 2021, with around 80% denominated in US dollars and 9% in sterling.[8] Maturing bonds will reduce the scale of the problem in time, but there is a significant volume of maturities beyond 2030, and some bonds are perpetual, with no maturity date.[9] In addition, legacy bond contracts are difficult to change.

Transitioning individual bonds through consent solicitations

6 Consistent with the policy that those who can transition should do so, the Sterling Risk-Free Rate Working Group is keen to encourage the transition of as many legacy sterling LIBOR bonds as practicable to SONIA using market-based solutions, with the objective of reducing dependence on LIBOR and taking LIBOR risk out of the financial system before the permanent discontinuation of LIBOR. This is because the regulator has stated that LIBOR is certain to end, but that it is not possible at this stage to rely on legislation to solve the legacy sterling LIBOR bond problem.[10]

7 One way of addressing the legacy sterling LIBOR bond problem is to amend the interest rate provisions in bond contracts through a process of consent solicitation. This is an existing market practice for individual bonds. Issuers can propose to undertake consent solicitations if and when they wish. Successful completion is dependent on consent thresholds being met by a sufficient proportion of investors. Following ABP's pioneering transaction in June 2019, seven other consent solicitations were successfully completed in the second half of 2019 by Lloyds Banking Group, Santander and Nationwide with a value of £4.2 billion in total.[11] Successful consent solicitations and other liability management exercises – such as bond exchanges or buybacks – reduce the amount of legacy sterling LIBOR bonds outstanding.

8 Where sterling LIBOR is replaced by SONIA for outstanding legacy bonds, a fixed credit market adjustment spread is needed to address the economic differences between LIBOR and SONIA.[12] The credit adjustment spread used in consent solicitations to date is a market rate, based on the linear interpolation for the relevant tenor of LIBOR versus SONIA basis swaps, which is then added to the original margin of the legacy bond. Over the period between now and the permanent discontinuation of LIBOR, the market rate for consent solicitations may converge on ISDA's proposal for a fixed adjustment spread, using the median of the spread between LIBOR and risk-free rates over a five-year look-back period.[13] This is expected to be used in derivatives fallbacks on the permanent discontinuation of LIBOR.

6. Where derivatives are used to hedge legacy bond contracts which fall back to a fixed rate when LIBOR is permanently discontinued, there may be a hedging mismatch, as derivatives may fall back to an alternative rate in accordance with their own terms.

7. See Catherine Wade, Linklaters, *Fallbacks for LIBOR Floating Rate Notes,* ICMA Quarterly Report, Third Quarter 2019.

8. Source: RBC Capital Markets, October 2018.

9. However, it is relevant to note that the average life of some securitisations is significantly shorter than their final maturity, and some have call options.

10. Edwin Schooling Latter, Director of Markets and Wholesale Policy, FCA: "The best way to avoid LIBOR-related risks is to move off LIBOR altogether.": *Next Steps in Transition from LIBOR,* Risk.net Summit, 21 November 2019.

11. Market sources.

12. Andrew Bailey, Chief Executive of the FCA: "Today we see no prospect of the administrator being able to continue with a dynamic credit spread – the likely choice would be between a risk-free rate plus fixed spread, or nothing. In other words, this does not provide a route to making LIBOR representative again.": *LIBOR: Preparing for the End:* New York, 15 July 2019.

13. See Edwin Schooling Latter, *Next Steps in Transition from LIBOR:* Risk.net LIBOR Summit, 21 November 2019.

Consent solicitations from LIBOR to SONIA under English law[14]

A bond is a contract between an issuer and bondholders (and the trustee for the bond, where relevant), which can only be amended with the consent of the parties, in accordance with the bond's terms and conditions.

Under English law, amendments to interest rate provisions in bond terms and conditions are usually "reserved matters" or "basic terms modifications" which typically require a quorum of two-thirds or 75% of holders of the outstanding principal amount of bonds, of which 75% have to vote in favour of the extraordinary resolution to amend the relevant terms and conditions. For an adjourned meeting or a reserved matter, a quorum of one-third or 25% of holders of the outstanding principal amount of bonds is required (if the first meeting is adjourned for want of quorum), of which 75% have to vote in favour of the extraordinary resolution to amend the relevant terms and conditions.

The provisions of each relevant legacy bond transaction need to be checked to ensure that any consent solicitation is conducted in accordance with its terms and conditions, including as to quorum and consent thresholds.

Issuers of floating rate notes may undertake a consent solicitation exercise to amend the interest rate provisions in the terms and conditions of legacy bond transactions (eg Type 1 legacy LIBOR bond contracts) so that they reference another rate in future (eg SONIA plus an adjustment spread).

As an alternative, issuers may undertake a consent solicitation exercise to amend the Type 1 fallback provisions in their legacy bond transactions so that the fallbacks to the risk-free rate are triggered on the occurrence of a specific event, such as the permanent discontinuation of LIBOR (akin to a Type 2 fallback), or the declaration that LIBOR is no longer representative (akin to a Type 3 fallback).

In the case of securitisations, consent solicitations need to be analysed on a tranche-by-tranche basis. It may be possible to group together series of securitisations when voting but, given the significance of a change to the interest rate, it is expected that the changes would need to be voted on tranche-by-tranche.

As a matter of market practice, irrespective of whether the underlying contracts formally require it, any consent solicitation proposal for securitisations would need to include a confirmation that the ratings on the relevant securitisation are unaffected.

A consent solicitation of a securitisation requires the involvement of the issuer, the trustee and other transaction parties, including the originator. While the directors of SPVs (special purpose vehicles, the issuers of the securitisations) may be prepared to engage with the trustee and put a proposal to a vote of holders of the securitisation, there may be concerns about whether the structure can bear the cost where the originator or sponsor is not willing to fund such costs itself.

In the European securitisation market, AFME has developed model benchmark rate modification language[15] to allow changes to be made to terms and conditions of securitisations via a simplified consent mechanism with the involvement of the trustee (so-called "negative consent" wording). This negative consent mechanism has not been adopted elsewhere in the bond market.

14. It is also important to note that the Sterling Risk-Free Rate Working Group is expected shortly to publish a statement and considerations relating to consent solicitations from LIBOR to SONIA so far. These considerations will be kept under review as the market continues to develop.

15. AFME, *Benchmark Rate Modification Language*.

Transitioning the legacy bond market as a whole

9 Transitioning the legacy bond market *as a whole* – involving FRNs, covered bonds, capital securities and securitisations – through consent solicitations and other liability management exercises would be a long, complex and costly process.[16] In the UK, the growing experience of consent solicitations to date may help to streamline the process. But individual bond contracts will still need to be amended, bond by bond. (A protocol cannot be used to change legacy bond market contracts, unlike the protocols used by ISDA in the derivatives market.)

10 There are two main constraints limiting the ability to transition the legacy bond market as a whole by the end of 2021:

- *Feasibility:* The first constraint is that, even though consent solicitations and other market-based solutions are being encouraged wherever possible, some bonds may be too difficult to transition from LIBOR to SONIA: for example, consent thresholds are often high and individual bonds – which are freely transferable – are often held by many investors, not all of whom can necessarily be identified; the process is voluntary, so some issuers may decide not to convert; some securitisations may in practice have no decision-taker; and regulatory capital may prove difficult to convert. This would leave a rump of unconverted bonds still referencing LIBOR.
- *Time:* The second constraint is that, even where transition is possible in principle, there are likely in practice to be too many bonds to transition from LIBOR to SONIA before the end of 2021, given the time needed to undertake consent solicitations, bond by bond.

11 It is also relevant to note that, in the US, consent thresholds for legacy bonds referencing LIBOR are commonly 100%. Given that the identity of bondholders is not always known, consent solicitation in the US may not be practicable.[17]

A declaration by the FCA that LIBOR is no longer representative

12 It is already clear that some banks will leave LIBOR panels at, or shortly after, the end of 2021.[18] This will require the FCA, as regulator of LIBOR, to make a judgment about whether LIBOR is still representative of its underlying market under the EU Benchmarks Regulation (BMR). If and when the FCA declares LIBOR to be no longer representative and LIBOR is no longer registered under the BMR, supervised entities will no longer be able to use LIBOR for new debt and swap transactions.[19] The FCA has stated that "the potential solution of allowing continued publication of LIBOR for use in legacy instruments that do not have mechanisms to remove their dependence on LIBOR could help to prevent otherwise unavoidable disruption in cash markets."[20]

13 If LIBOR can continue to be used for legacy bonds after a declaration by the FCA that LIBOR is no longer representative, this will reduce the amount of legacy bonds outstanding at the time of the permanent discontinuation of LIBOR by giving more time for more bonds to mature, and it may also provide an opportunity for more consent solicitations to take place.[21] But the administrator and the banks quoting LIBOR may be reluctant to quote an unrepresentative rate without approval from the authorities, or to continue to do so for a long period. So this approach is unlikely to work for very long, particularly if banks decide subsequently to withdraw.[22]

16. Preliminary market estimates indicate that that there are around of 750 ISINs for bonds referencing sterling LIBOR across 438 deals, with a value of around £110 billion. These figures should be regarded as broad orders of magnitude, not precise estimates.

17. It is understood that there are no current plans to replace EURIBOR, though €STR will be built into fallbacks for new EURIBOR bond contracts, and €STR may be used for new floating rate euro-denominated bond issues (as already pioneered by the EIB).

18. Andrew Bailey, Chief Executive of the FCA: "We do expect panel bank departures from the LIBOR panels at end-2021.": *LIBOR: Preparing for the End,* New York, 15 July 2019.

19. EU BMR, Article 29(1). See also the letter from FSB Official Sector Steering Group Co-Chairs to ISDA: "While the EU BMR envisages circumstances in which a critical benchmark that has infringed the provisions of the Regulation may continue to be published to avoid a disruptive cessation and potential financial instability, it also envisages that EU supervised entities would no longer be able to enter into new derivative or securities transactions referencing LIBOR in those circumstances.": 15 November 2019.

20. Edwin Schooling Latter, Director of Markets and Wholesale Policy, FCA: *LIBOR Transition and Contractual Fallbacks,* ISDA Annual Legal Forum, 28 January 2019.

21. If or when the FCA declares that LIBOR is no longer representative, only Type 3 legacy bond contracts (ie those with Type 2 fallbacks plus a pre-cessation trigger) would be transitioned to SONIA.

22. Edwin Schooling Latter, Director of Markets and Wholesale Policy, FCA: "Even if some panel banks were willing to continue, it would not be comfortable for them – I imagine they would want to keep the period in which they continued submitting as short as they could. It will not be comfortable for the administrator of the rate.": *Next Steps in Transition from LIBOR:* Risk.net LIBOR Summit, 21 November 2019.

As an alternative, changing the method of calculating LIBOR would be likely either to depend on an initiative by the administrator or require the intervention of the authorities.[23]

Permanent discontinuation of LIBOR

14 At the permanent discontinuation of LIBOR, many legacy bonds still outstanding will fall back to a fixed rate (ie the last LIBOR fix) unless the authorities have decided to intervene (eg by using their regulatory powers or through new legislation.) The FCA has stated that it is sensible to consider the pros and cons of legislation, and to see if and where a consensus exists. But the FCA has made it clear that the market should *not* work on the assumption that legislation will be introduced; it is not a "magic wand"; it is not within the gift of the regulators; and it is not clear what the position in Parliament (or other jurisdictions) would be.

Pros and cons of official intervention, if feasible

15 The first question to consider from a bond market perspective is whether there is a significant risk of market disruption that would justify intervention by the authorities, if intervention is feasible. There are a number of important considerations to assess:

- *Fairness:* The permanent discontinuation of LIBOR was not contemplated when Type 1 LIBOR bond contracts were written before July 2017. Where these contracts are outstanding at permanent discontinuation, they will fall back to a fixed rate (ie the last LIBOR fix). This was not the original intention of the parties, even though the terms of the contract are quite clear. If the contracts fall back to a fixed rate (ie the last LIBOR fix), the result is likely to put either issuers or investors at a disadvantage, and quite possibly both.[24] As permanent discontinuation was not contemplated when the bonds were issued, there is a risk of market disruption if market participants challenge the outcome on the grounds that they do not consider that it is fair.[25]
- *Feasibility of transition:* The authorities have encouraged the market to transition from LIBOR to risk-free rates as soon as possible, where they can. But in some cases, this is not likely to be feasible, as the contracts cannot be changed: eg because consent thresholds cannot be reached. In others, there is not likely to be time to change them all by the end of 2021, because there are large numbers of outstanding bonds and each bond needs to be transitioned separately, bond by bond, which is a time-consuming process.[26] As consent solicitations are typically a voluntary initiative by issuers, investors may not have an opportunity to transition their bonds unless issuers agree. They may be able to sell their bonds in the market, but this could have a significant effect on the market price.
- *Variety of fallback clauses in financial contracts:* While Type 1 bond contracts will fall back to a fixed rate (ie the last LIBOR fix) on permanent discontinuation of LIBOR, there may be other bond contracts which have no fallbacks at all, or the fallbacks may not be effective. This is not just a risk in the bond market; it may be a feature of other financial products as well.
- *International consistency:* In the US, where consent solicitation is not expected to be practicable, as consent thresholds are commonly 100%, it is understood that the feasibility of legislative relief is being explored.[27] If there

23. European Commission: "Alongside the power to compel the administrator of a critical benchmark to continue publication, it might be useful for the competent authorities to have, also in these circumstances, the power to require the necessary changes to the benchmark's methodology.": *Review of the EU BMR,* October 2019.

24. £ RFR Working Group: "In the context of a permanent discontinuation of LIBOR, this would effectively result in the floating rate bonds becoming fixed rate bonds, because the last determined rate would be applied for the remainder of the life of the bond. This may be commercially unacceptable for both issuer and investors. From an investor perspective, such issues may become illiquid and may cease to perform the commercial purpose investors intended for them. From an issuer perspective, those that aim to match liabilities via other instruments may be adversely affected.": July 2018.

25. See, for example, the FCA (footnote reference above): "The potential solution of allowing continued publication of LIBOR for use in legacy instruments that do not have mechanisms to remove their dependence on LIBOR could help to prevent otherwise unavoidable disruption in cash markets." See also the European Commission, *Review of the EU BMR: Public Consultation Document,* October 2019: "On the basis of current estimates, contracts will be referencing IBOR rates at least until 2050. Certain contracts referencing IBOR rates might be impossible to change (eg mortgages or bonds with a 100% noteholder agreement clause). Should a critical IBOR rate cease, there is a risk of disruption to parties whose contracts reference this IBOR rate."

26. If the authorities decide not to intervene, it would still be possible after the permanent discontinuation of LIBOR for issuers to undertake consent solicitations under their existing legal contracts. But the economic terms would be different from the economic terms when the contracts were originally written because the contracts would involve transitioning to SONIA from a fixed rate for the remaining term of each contract rather than from a floating rate (ie LIBOR).

27. See Edwin Schooling Latter: "In the United States, where bond conversions are harder because they often require unanimous consent, the ARRC has been exploring whether there is a legislative option to build pre-cessation triggers into these contracts.": *Next Steps in Transition from LIBOR,* Risk.net LIBOR Summit, 21 November 2019.

is legislative relief for legacy bond contracts under New York law, US dollar bond contracts under New York law may be treated differently from US dollar bond contracts under English law, unless legislation is also considered in the UK.

Potential forms of official intervention, if feasible

16 In the US, the Alternative Reference Rates Committee (ARRC) is exploring whether to seek legislative relief under New York law for a proposal based on an ARRC-recommended SOFR rate and spread adjustment to LIBOR contracts governed by New York law across all asset classes, including LIBOR-based fallbacks to the last LIBOR fix (ie a fixed rate). Under the ARRC's proposal, potential legislative relief would:

- apply to all asset classes;
- apply to legacy contracts that are silent as to fallbacks;
- override legacy contract fallbacks if the legacy fallback is to a LIBOR-based rate (such as the last quoted LIBOR fix);
- *not* override legacy contract fallbacks to an express non-LIBOR-based rate (such as prime);
- provide a statutory safe harbour to parties who have the right to exercise discretion or judgment regarding fallbacks;
- allow parties to opt out of the application of the statute in writing at any time before or after the occurrence of a trigger event;
- provide a safe harbour to parties who add conforming changes to their documents to accommodate administrative/operational adjustments for the statutory endorsed benchmark rate; and
- apply or be available on the occurrence of statutory trigger events: for cash products, these would be based on the ARRC permanent cessation and pre-cessation trigger events; and for derivatives, they would be based on what ISDA does.[28]

17 If the ARRC proposal for SOFR were to be feasible under New York law, could it be adapted to SONIA under English law? There would be a range of precedents on which the authorities could draw, if they were willing and able to use their regulatory powers[29] or to introduce new legislation to determine that outstanding legacy LIBOR contracts in sterling would be read as (or deemed to be) SONIA plus a fixed adjustment spread.

- If this outcome was achieved by using regulatory powers to modify the methodology for calculating LIBOR so that LIBOR were to become SONIA plus a fixed spread, the approach would have some similarities with the statement by the ECB, following a recommendation by the Euro RFR Working Group, that from 2 October 2019 the method of calculating EONIA should be modified so that it is defined as €STR plus a fixed adjustment spread (of 8.5 basis points) for a transition period until 3 January 2022.[30] But it is important to note that the transition from EONIA to €STR is from one overnight rate to another, whereas the transition from LIBOR to compounded SONIA would be from a forward-looking term rate (ie LIBOR) to a backward-looking overnight rate (ie compounded SONIA).
- If the outcome was achieved by introducing legislation which would override contractual references to LIBOR so that they are read as (or deemed to be) references to SONIA plus a fixed spread, the approach would have similarities with the introduction of the euro in place of the national currencies of relevant EU Member States at fixed conversion rates on 1 January 1999, where references in contracts to the relevant national currency were read as references to the euro at the relevant fixed conversion rate.[31]

18 From the perspective of the bond market, the challenge would be to ensure that, on permanent discontinuation of LIBOR, (i) ISDA derivative contracts would fall back to compounded SONIA plus a fixed adjustment spread, as planned, while (ii) Type 1 bonds referencing LIBOR would be read as compounded SONIA plus a fixed spread instead of falling back to a fixed LIBOR rate (ie the last LIBOR fix), so that (i) and (ii) would have the same effect.

28. US Alternative Reference Rate Committee (ARRC) minutes for the 15 November 2019 meeting.

29. The scope of regulatory powers under the EU Benchmark Regulation is currently subject to review. See European Commission, *Review of the EU Benchmark Regulation*, October 2019.

30. From 2 October 2019, "EONIA will be calculated as the €STR plus a spread. On 31 May 2019, the ECB provided the market with a one-off calculation of the spread between the €STR and EONIA that will be used for the calculation of EONIA. This spread will remain fixed at the level computed and published by the ECB until the final discontinuation of EONIA." Source: European Money Markets Institute (EMMI), 31 May 2019. The value of this one-off spread, as computed and published by the ECB is 0.085% (ie 8.5 basis points).

31. Under EC/1003/97: "[On 1 January 1999] the euro will be substituted for the national currency of each participating Member State at the conversion rate." … "At the end of the transition period (on 31 December 2001), contracts will be read as if all references to participating national currency units were to euro units at the conversion rates." And under EC/974/98: "Continuity and freedom of contact are safeguarded." Source: Bank of England, *Practical Issues Arising from the Introduction of the Euro,* No. 10, December 1998.

19 However, the feasibility of an approach of this kind would require a number of issues to be addressed. For example:

- It would need to be determined whether it would legally be possible to override existing bond contracts, the terms for which are quite clear in the bond documentation, even though the outcome of the fallback (ie a fixed rate bond) was not the original intention of the parties. In addition, any legislation would need to override contractual provisions relating to the timing and method of calculating interest, and not just references to LIBOR. This is because interest on legacy bonds referencing LIBOR is fixed at the start of the interest period, whereas the interest rate on compounded SONIA would only be available near the end of the interest period.
- If legislation could be used to override existing contracts, the provisions in the legislation – that references to LIBOR would be read as compounded SONIA plus a fixed spread – would apply to all LIBOR fallbacks, not just fallbacks to a fixed rate, unless there was provision in the legislation for exemptions. Some users of legacy products such as loans and mortgages – eg retail and small business users – might prefer to fall back to a term SONIA rate or base rate rather than a compounded SONIA rate, and provision might need to be made for this. Some of these alternative rates might be proprietary, and questions about intellectual property rights might arise.

International coordination

20 Finally, as LIBOR is used globally in contracts governed by a range of different laws in different jurisdictions, official intervention would preferably need to be agreed internationally and coordinated globally (eg by the FSB Official Sector Steering Group) for all jurisdictions using LIBOR, especially the US, which would represent the largest component. Work would take a considerable period to plan, and the market would need to be consulted.

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Key publications on the global transition to risk-free rates

By Charlotte Bellamy and Katie Kelly

RFR

As the end of 2021[1] draws closer, developments in the transition to risk-free rates from LIBOR are picking up speed and authorities and other bodies involved in the transition are frequently publishing relevant materials. This article seeks to draw together and summarise the most important recent publications for the bond market. It follows a similar article in the Third Quarter 2019 edition of this Quarterly Report, which summarised key publications from the first half of 2019.

The key publications are organised by theme as follows: (i) adoption of risk-free rates in the international bond market; (ii) fallbacks; (iii) regulatory, tax and other matters; (iv) the development of term risk-free rates; and (v) developments in relation to the EU Benchmarks Regulation (EU BMR), including a summary of ICMA's response.[2]

These are preceded by a box introducing key recent official speeches regarding the transition to risk-free rates. Other publications on the transition to risk-free rates are summarized in a box in the International Regulatory Digest section of this Quarterly Report.[3]

1. The end of 2021 is the date from which continued publication of LIBOR cannot be guaranteed.

2. For information on the transition of legacy LIBOR instruments to risk-free rates, please see the Quarterly Assessment on *The Transition from LIBOR to Risk-Free Rates: Legacy Bonds* in this Quarterly Report.

3. For information and publications on the transition from EONIA to €STR, please see the article *Euro risk-free rate reform* in the Fourth Quarter 2019 edition of this Quarterly Report.

Key official speeches regarding LIBOR and EURIBOR

- *LIBOR: Preparing for the End*, a speech by Andrew Bailey, Chief Executive of the FCA, given on 15 July 2019. Andrew Bailey noted that transition from LIBOR has made good progress across derivatives and securities markets, and transition in loan markets is a key next step. He set out the benefits to borrowers of the move to risk-free interest rate benchmarks and noted that UK lenders will need to begin engaging with borrowers about lending based on these rates. He also highlighted that the FCA expects the LIBOR panels to dwindle or disappear after end-2021, so firms must be able to run their business without LIBOR from this date and reduce the stock of "legacy" LIBOR contracts. Regarding legacy contracts that cannot be converted away from LIBOR or have fallbacks added (the "tough legacy" question), he said that, although legislative solutions are not within the gift of the regulators, "it is sensible to consider their pros and cons".
- *LIBOR: The Clock is Ticking*, a speech by John C. Williams, President and Chief Executive Officer of the Federal Reserve Bank of New York, given on 23 September 2019. The speech highlighted the urgency of the need to move away from LIBOR, progress made in adoption of SOFR and challenges ahead. Separately, in his remarks at a Managed Funds Association conference, John C. Williams addressed what the variability in repo markets means for SOFR. He said that the temporary SOFR spike in autumn 2019 was unsurprising because "SOFR reflects rates on real-world transactions," and he explained that financial contracts generally refer to an average of SOFR over time. He noted that the spike should not be used as an excuse to delay transitioning away from LIBOR because "like death and taxes, the end of LIBOR is unavoidable, and we must do all that it takes to prepare for a LIBOR-less future."
- *Join the Revolution! Why it Makes Business Sense to Move On from LIBOR*, a speech by Andrew Hauser, Executive Director for Markets, Bank of England, given on 27 June 2019. Andrew Hauser looked at the opportunities a post-LIBOR world could offer. He also set out how the Bank of England is adapting its own operations to the use of SONIA.
- The *Second Roundtable on Euro Risk-Free Rates* at the ECB on 25 September 2019 included an opening speech by Benoît Cœuré, Member of the Executive Board of the ECB.
- *Ongoing Reforms and Challenges Ahead*, a speech by Steven Maijoor, Chair of ESMA, given on 29 October 2019. The speech discussed ESMA's role under the EU BMR and more generally in the global reform of interest rates. He said: "There is a clear commitment by the administrator of EURIBOR and the public sector to sustain EURIBOR and the work will continue in the next years to ensure that the panel of banks contributing to EURIBOR is stable and representative. ... Just as for all benchmarks authorised under the Regulation, fallback clauses are needed for EURIBOR too. This is because users, and their clients, should be able to know in advance what will happen to their contracts if EURIBOR ceases to be provided."
- *Next Steps in Transition from LIBOR*, a speech by Edwin Schooling Latter of the UK FCA, given on 21 November 2019. The speech covered the key next steps in reducing the risks from continued use of LIBOR, highlighting "In sterling IRS (interest rate swap) markets, we will be encouraging market makers to make SONIA the market convention from Q1 2020" and "The sterling RFR Working Group has set a target of Q3 2020 to stop new lending using LIBOR." He also stated: "The conduct risks of striking new LIBOR-referencing transactions that endure beyond end-2021 are rising"; and he discussed pre-cessation triggers, noting that the arguments for a pre-cessation trigger seem persuasive.
- *Introductory Remarks* by Andréa Maechler, Board member of the Swiss National Bank, given on 12 December 2019, called upon market participants to implement the recommendations of the National Working Group on Swiss Franc Reference Rates in relation to the transition from CHF-LIBOR to SARON and noted that the successful transitioning away from CHF-LIBOR hinges on the development of more SARON-based cash products.

There has been good progress in the adoption of risk-free rates in bond markets.

Adoption of risk-free rates in the international bond market

There has been good progress in the adoption of risk-free rates in bond markets. Key developments include:

- The Working Group on Sterling Risk-Free Reference Rates (£RFR Working Group) published a *Statement on Conventions for Referencing SONIA in New Contracts and Summary of Responses to Discussion Paper* in August 2019. The Statement noted that the £RFR Working Group considers it sensible for cash market conventions to align with existing OIS market conventions where possible, namely compounded average settled in arrears. In addition, the £RFR Working Group views the 5-day lag period used in the SONIA bond market as sensible. Further information can be found in the article *Risk-Free Rates: Bond Market Conventions* in the Fourth Quarter 2019 edition of this Quarterly Report.
- The ECB published the €STR (the new €RFR) for the first time on 2 October 2019, reflecting trading activity on 1 October 2019. This first setting was determined as -0.549% and was reported as being based on 432 transactions from 32 active banks. Alongside this, on 2 October, EMMI, for the first time, published EONIA (for 1 October) under the reformed determination methodology (ie €STR + 8.5bp, giving a rate of -0.464%, as compared to an announced EONIA rate for 30 September of -0.451%). EMMI also announced that it had applied for authorisation of EONIA from the Belgian FSMA, under Article 34 of the EU BMR and subsequently, on 11 December, announced that this authorisation had been duly granted. EMMI published its *EONIA Benchmark Statement* on 18 December 2019. EMMI will continue to publish EONIA every TARGET day until 3 January 2022, the date on which this benchmark will be discontinued.
- The first bonds referencing €STR were issued after €STR publication began on 2 October 2019. The first benchmark transaction was issued by the European Investment Bank: a €1 billion 3 year €STR bond.
- In the US, the Alternative Reference Rates Committee (ARRC) released an Appendix to the SOFR FRNs *Conventions Matrix*. The Matrix, which was issued in August 2019, identifies considerations relevant to using SOFR – the ARRC's recommended alternative to USD LIBOR – in new FRNs and supplements the ARRC's paper *A User's Guide to SOFR* released in April 2019. In conjunction with the Matrix, the ARRC had also released the *SOFR FRNs Comparison Chart*, which outlines conventions already being used in the market. The Appendix builds upon these documents and is intended as an additional resource for market participants to consider.
- In addition, the Federal Reserve Bank of New York, in order to support a successful transition away from USD LIBOR, and as administrator of SOFR, in cooperation with the Treasury Department's Office of Financial Research, requested comments on a proposal to publish daily three compounded averages of SOFR with tenors of 30-, 90-, and 180-calendar days, and to publish daily a SOFR index that would allow the calculation of compounded average rates over custom time periods. This development was welcomed by the ARRC.
- In Asia Pacific, issuance of bonds referencing alternative RFRs has begun with, among others, Bank of China issuing a floating rate note based on SOFR and the South Australian Government Financing Authority issuing two floating rate notes based on AONIA.
- The Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks published a report on the results of its consultation on JPY interest rate benchmarks on 29 November, together with a summary of the main points and a press release. In respect of bonds, there was a general preference among respondents for term rates to replace JPY LIBOR, although for the bond market there were "a relatively large number of respondents" who envisaged using TONA compounded in arrears. However, responses indicated that a sufficient period for preparation would be necessary in order to make

necessary adjustments to business operations and systems, as well as trading practices, in order to use TONA compounded in arrears.

- In August 2019, the Association of Banks in Singapore and the Singapore Foreign Exchange Market Committee issued a consultation report that identified the Singapore Overnight Rate Average (SORA) as the alternative interest rate benchmark to the SGD Swap Offer Rate (SOR) (which is linked to USD LIBOR) and set out a roadmap for this transition. On the same day, the Monetary Authority of Singapore announced the establishment of a Steering Committee to drive transition from SOR to SORA.

Separately, the Loan Market Association published for its members exposure drafts of a compounded SONIA-based sterling term and revolving facilities agreement and a compounded SOFR-based dollar term and revolving facilities agreement in September 2019. The documents do not constitute recommended forms of the LMA; they have been published as exposure drafts which are open for comments from market participants.

Fallbacks

In addition to referencing risk-free rates in new bonds, authorities and market participants are also focused on fallbacks to IBORs and other reference rates:

- *GBP-LIBOR cash product fallbacks:* The £RFR Working Group published a *Consultation on the Credit Adjustment Spread Methodologies for Fallbacks in GBP LIBOR Cash Products* in December 2019. The paper considers four methodologies that could be used to calculate the credit adjustment spread for fallback language in sterling cash instruments. The deadline for responses is 6 February 2020.
- *USD-LIBOR cash product fallbacks:* The ARRC published a summary of its USD-LIBOR fallback language in November 2019.
- *EURIBOR fallbacks:* The Working Group on Euro Risk-Free Rates (Euro RFR Working Group) published high level recommendations for fallback provisions in contracts for cash products and derivatives transactions referencing EURIBOR in November 2019. The Euro RFR Working Group recommends that market participants consider incorporating fallback provisions in all new financial instruments and contracts referencing EURIBOR, regardless of whether they fall within the scope of the EU BMR. There are a set of general recommendations relating to the approach that may be taken in relation to EURIBOR fallbacks and some suggested language. The Euro RFR Working Group is also working towards the publication of certain consultations and resulting recommendations relating to EURIBOR fallbacks in H1 2020, as detailed in this timeline of deliverables of the Euro RFR Working Group.
- *€STR fallbacks:* The Euro RFR Working Group also published a report on €STR fallback arrangements in November 2019. The purpose of the report was to provide supervised entities with guidance on potential ways to comply with Article 28.2 of the EU BMR when using €STR as the euro risk-free rate in contracts.
- *IBOR fallbacks in derivatives:* ISDA published a report that summarises responses to a consultation on the final parameters of adjustments that will apply to derivatives fallbacks for certain IBORs in November 2019. The report follows two earlier consultations that found the overwhelming majority of respondents preferred the compounded setting in arrears rate to address differences in tenor between IBORs and overnight risk-free rates, and the historical mean/median approach to deal with differences in credit risk and other factors. Responses to the final parameters consultation show that a majority of participants preferred a historical median approach over a five-year lookback period. A majority also preferred not to include a transitional period in the spread adjustment calculation, not to exclude outliers, and not to exclude any negative spreads. For the compounded setting in arrears rate, a clear majority favoured a two-banking-day backward shift adjustment for operational and payment purposes. ISDA also announced in July 2019 that Bloomberg Index Services Limited had been selected to calculate and publish adjustments related to fallbacks that ISDA intends to implement for certain interest rate benchmarks in its 2006 ISDA Definitions.

  ISDA also launched in December 2019 a supplemental consultation on the spread and term adjustments that would apply to fallbacks for derivatives referencing euro LIBOR and EURIBOR, in the event those benchmarks are permanently discontinued, with a deadline of 21 January 2020. The consultation also covers technical issues related to the adjustment methodology and seeks feedback on whether the adjustments would be appropriate for lesser-used IBORs if ISDA implements fallbacks for those benchmarks in the future.
- *IBOR fallbacks in derivatives – pre-cessation issues:* ISDA also published a report summarising responses to a consultation on pre-cessation issues for LIBOR and certain other IBORs in October 2019. The responses indicated that a majority of market participants would generally not want to continue referencing a covered IBOR in existing or new derivatives contracts following a statement from a supervisor that it is no longer representative of the underlying market. However, the consultation did not reveal a consensus on how to respond to such a statement in the context of fallbacks

for derivatives contracts. This was followed by a letter dated 19 November 2019 from the Official Sector Steering Group of the FSB, which encouraged ISDA to add a "pre-cessation" trigger alongside the cessation trigger as standard language in the ISDA definitions for new derivatives and in a single protocol, without embedded optionality, for outstanding derivative contracts referencing key IBORs. According to the letter, this would help to reduce systemic risk and market fragmentation by ensuring that as much of the swaps market as possible falls back to alternative rates in a coordinated fashion. ISDA responded to the FSB's letter on 4 December 2019, calling for, among other things, greater clarity on certain points to assist market participants in understanding the implications of a "non-representative" LIBOR, including a confirmation from the FCA and the administrator for LIBOR that a "non-representative" LIBOR would only be published for a short period (ie a number of months, not years).

Regulatory, tax and accounting matters

The past six months have seen a high level of focus on regulatory, tax, accounting and other issues connected with the transition to risk-free rates from LIBOR. Key publications are summarised below:

- In July 2019, the Euro RFR Working Group wrote a letter to the International Accounting Standards Board (IASB) to inform IASB of the objective and status of the reform agenda regarding interest rates in the euro area and to express some concerns in relation to potential accounting issues triggered by the reform based on the analysis of the potential IFRS accounting issues.
- In September 2019, the IASB amended some of its requirements for hedge accounting to provide relief from potential effects of the uncertainty caused by the IBOR reform. In addition, the amendments require companies to provide additional information to investors about their hedging relationships which are directly affected by these uncertainties.
- In October 2019, the £RFR Working Group published letters to the UK Prudential Regulation Authority, UK Financial Conduct Authority, European Commission and Basel Committee on Banking Supervision regarding regulatory barriers to transition away from LIBOR. The letters request that the issues raised are considered and concrete actions are taken where necessary to ensure a smooth transition away from LIBOR. The £RFR Working Group also wrote to EIOPA in July 2019 to encourage EIOPA to remove the recognised Solvency II barriers to transition.

  Subsequently, the FCA answered key questions on conduct risk arising from LIBOR transition in November 2019, outlining (among other things) their expectation that firms have a strategy in place and take necessary action during LIBOR transition, and customers are treated fairly by following their rules and guidance.

  The PRA responded to the Sterling RFR Working Group's letter in December 2019. In particular, the PRA noted, in relation to AT1 and Tier 2 Capital, that it does not believe it is desirable to reassess the eligibility of instruments where the amendments are solely to replace the benchmark reference rate. The PRA has made this point at the Basel Committee on Banking Supervision and is making progress towards achieving an internationally consistent response. The PRA also noted that its rules on Contractual Recognition of Bail-In and Stay in Resolution could be considered relevant where legacy contracts are judged to have been materially amended. The PRA is considering possible implications of benchmark rate reform for those rules and plans to provide an update in spring 2020.
- In October 2019, the ARRC issued a press release welcoming the US Department of the Treasury and the Internal Revenue Service's release of proposed regulations providing tax relief related to issues that may arise as a result of the modification of debt, derivative, and other financial contracts from LIBOR-based language to alternative reference rates.
- In November 2019, the Financial Accounting Standards Board (FASB) approved an Accounting Standards Update (ASU) to provide temporary, optional guidance to ease the potential burden in accounting for, or recognising the effects of, reference rate reform on financial reporting. The Board is expected to issue a final ASU in early 2020.
- The Euro RFR Working Group released a report in November 2019 on the financial accounting implications of the transition from EONIA to the €STR, and the introduction of €STR-based fallbacks for EURIBOR. The report primarily focuses on the EU BMR implications for hedge accounting related topics, and challenges for non-hedge related topics, and sets out relevant key recommendations.
- In December 2019, the UK Financial Reporting Council issued *Amendments to FRS 102 – Interest Rate Benchmark Reform* to provide relief to aid the transition from LIBOR to SONIA. The amendments are effective for accounting periods commencing on or after 1 January 2020.

Term rates

While new bonds referencing risk-free rates have generally adopted an average setting in arrears approach, work is underway to develop term rates in the UK, US, euro area and Japan. It is understood that such term rates are expected to be used in a limited sub-set of financial products, such as certain loans and mortgages, trade and working capital, Islamic finance. Recent publications relating to the development of term rates include:

- The Euro RFR Working Group published a call to benchmark administrators for expressions of interest in producing a €STR-based forward-looking term structure in July 2019. Five administrators duly responded to the Working Group's call and their presentations are available on the ECB's website.
- The Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks released a statement soliciting potential future administrators of JPY term reference rates in October 2019. It subsequently closed the call for applications on 31 December 2019, as it had received sufficient applications from entities with relevant experience.

Developments in relation to the EU Benchmarks Regulation

There have also been several recent developments relating to the EU Benchmarks Regulation (EU BMR):

- The European Commission published a consultation paper requesting comments on various aspects of the EU BMR including in the areas of IBOR reform, orderly cessation of a critical benchmark, authorisation and registration of benchmarks, the scope of the EU BMR, third country, climate-related and commodity benchmarks in October 2019. For information on ICMA's response to this consultation, please see the box below.
- Also in October 2019, ESMA and the Australian Securities and Investments Commission (ASIC) announced that they had signed a Memorandum of Understanding setting out cooperation arrangements in respect of Australian benchmarks. In conformance with the EU BMR, this will allow benchmarks declared significant by ASIC (BBSW, S&P/ASX200, Bond Futures Settlement Price, CPI, and Cash Rate) to be used in the EU by EU-supervised entities.
- ESMA is publishing registers of administrators, with over 70 now duly registered, and third country benchmarks, with in excess of 80,000 benchmarks now duly registered, in accordance with the EU BMR. ESMA has also published a table, last updated on 8 October, showing which applicable EEA competent authorities comply, or intend to comply, with ESMA's *Guidelines on Non-Significant Benchmarks under the EU BMR*.
- Various amendments to the EU BMR as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and Sustainability-related disclosures for benchmarks were published in the *Official Journal* and entered into force in December 2019. As part of this package of changes, the maximum period of mandatory administration and contribution for critical benchmarks was extended from two years to five years and the transition period in the original EU BMR was extended from end 2019 to end 2021 for both critical and third country benchmarks.
- ESMA published updated *Q&A on the EU BMR* in December 2019, which included new Q&As related to, among other things, (a) the role and responsibilities of a legal representative under Article 32(3) of the EU BMR (Recognition of an administrator located in a third country) and (b) transitional provisions applicable to third country benchmarks.
- ESMA also published a *Briefing on the Implementation of the Recognition Regime under Article 32 of the EU BMR* in December 2019, which aims to clarify some aspects of the recognition application such as: (a) the means to determine the Member State of reference; and (b) the instances where cooperation arrangements between EU and third-country competent authorities are needed.
- Finally, ESMA published a statement regarding pending applications by EU administrators of benchmarks in December 2019. The statement includes a table of information shared by NCAs with ESMA in relation to the applications for authorisation and registration by EU administrators under Article 51.1 of the EU BMR for which the decision by the relevant NCA is still pending. Under Article 51.3 of the EU BMR, EU supervised entities can continue to use existing benchmarks provided by the administrators included in the table unless and until such authorisation or registration is refused.

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ICMA's response to the European Commission's consultation on the EU Benchmarks Regulation

ICMA submitted a response to the European Commission's consultation paper on the EU Benchmarks Regulation (EU BMR) in December 2019. A summary of the key points in ICMA's response is set out below.

Critical benchmarks and IBOR reform and cessation

- Broader powers for competent authorities to require the administrator to change the methodology of a critical benchmark could help to ensure continuation of critical benchmarks and thereby avoid market disruption which could occur upon the cessation of a critical benchmark such as LIBOR or EURIBOR.
- However, it will be very important that competent authorities and administrators are mindful of the need to support contractual continuity as far as possible if the methodology of a benchmark is modified.
- Any broader powers should be confined to situations in which mandatory administration or contribution to a critical benchmark is triggered.
- It is not clear whether it is necessary to mandate pre-cessation triggers in the EU BMR given existing market practice and other initiatives in this area. If the inclusion of pre-cessation triggers in contracts is mandated, this should not have a retroactive effect and it must be drafted in a clear and objective way.

Authorisation and registration of benchmarks

- A drafting change to ensure it is clear that a competent authority has the power to withdraw or suspend authorisation or registration of an administrator in respect of one or more benchmarks only would be welcome.
- Continued publication and use of a benchmark should be allowed in certain specified circumstances when the authorisation of the administrator has been withdrawn (and not only suspended, as currently envisaged in the EU BMR).

ESMA register of administrators and benchmarks

- It would be helpful if the ESMA register were to list authorised benchmarks as well as administrators.

Non-EEA benchmarks

- ICMA's article, *The Impact of the EU BMR on the Use of Third Country Benchmarks,* noted several concerns with the third country regime under the EU BMR. Continued efforts to provide timely equivalence rulings, clear guidance and proportionate application of requirements can all contribute positively to assuaging the concerns. Consideration should also be given to expanding the definition of "public authority" to include third country administrators of FX spot rates in non-convertible and pegged currencies.
- It will be crucial that EU27 supervised entities are able to continue using LIBOR under the EU BMR in the event that LIBOR becomes a third country benchmark from an EU27 perspective, and conversely it will also be important that the other EU critical benchmarks continue to be available for use by supervised entities under a post-Brexit UK regime.

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Putting the capital in the European Capital Markets Union

By Joanna Cound, BlackRock

CMU Building deeper, better-connected capital markets in Europe is an important objective to promote investment, realise the goal of a true Single Market for capital, and help European savers and companies realise their long-term financial objectives.

A more engaged investor base not only represents a growing supply of capital for companies to tap for investment, but equally advances a number of key policy aims: reinforcing the Banking Union and European Monetary Union, underpinning the role of the euro globally, and meeting the European Union's (EU's) ambitious sustainable investment goals.

To date, the CMU has built a policy agenda which, when seen through to completion, will provide a framework for advancing this aim. But important challenges remain, and some of the remaining barriers will be difficult to break down, both technically and politically.

The most valuable way to add greater imperative to addressing these challenges is to refresh the CMU agenda so that it can deliver something meaningful and tangible for European citizens. The area of the original CMU agenda which has probably been the least developed is the one where we still believe the greatest dividend for Europe is to be found: a meaningful approach to incentivising savers to invest in capital markets which both brings more capital into European markets and, psychologically more important, delivers long term economic benefits to Europe's citizens as they plan for their futures.

A meaningful CMU agenda should focus on these three pillars:

- Pillar One: Promote retail investor participation by balancing investor protection and investor inclusion.
- Pillar Two: Maximise investors' utility from capital markets architecture.
- Pillar Three: Adopt a company-oriented vision for capital raising.

Pillar One: Promote retail investor participation by balancing investor protection and investor inclusion

Retail investment markets have changed significantly in recent years. Investor expectations continue to change (for example the growth of interest in sustainable investment), and regulatory reforms have brought notable structural changes to the way investment products are sold to end-investors. But providing investors with meaningful and efficient access to investment products and solutions remains a significant challenge.

In our annual Global Investor Pulse survey, we look at barriers to investing for European citizens. While some respondents do indeed show great risk-aversion, far more people cite barriers like access and lack of understandable information as a key barrier to investing their savings. Building off this, we propose five sets of policy principles to make it easier to invest in markets and empower citizens to achieve their long-term savings goals while maintaining enhanced levels of consumer protection.

(1) Simplifying the investment process by minimising the need for repeated know your client and take on procedures and overlapping documents and disclosures, which should be aggregated by the end service provider.

(2) Promoting the use of digital and interactive tools (not PDFs) for the purpose of (a) take on procedures, know your clients and suitability profiles, in order to increase point of sale engagement and education on key concepts; (b) creating a unique financial digital identity for every consumer; and (c) a personalised and portable fact find.

(3) Building on recent and upcoming regulatory redevelopments (such as MiFID II and the PEPP), standards on suitability must also evolve to recognise the importance of portfolio outcomes, rather than individual product outcomes, allowing a variety of

products to be included which meet an individual's long-term risk appetite as well as providing inflation protection.

(4) Focusing the value for money debate on the entire chain of distribution with meaningful comparability and transparency of products, advice, and distribution. Cost is only one aspect of value for money, as it needs to be read together with other key drivers of value such as performance, risk, and quality of service.

(5) Encouraging Member States' initiatives to drive increased investments, using for instance auto-enrolment to crowd savers into capital markets via diversified, risk-managed portfolios such as those being put in place under the PEPP.

Pillar Two: Maximise investors' utility from capital markets architecture

Today in Europe, once investor capital is invested in markets, it is generally channelled through market infrastructure which provides sub-optimal efficiency and protection for investors and their agents. An integral part of any reflection on the future of CMU, therefore, should be a consideration of the efficiency, safeguards, and costs of utilising European capital markets' architecture.

(1) One key area is transparency. Since the entry into application of MIFID II in January 2018, there have, from an investor perspective, been several notable improvements regarding the volume and breadth of data reported, but there is still some way to go to turn this data into useful information for investors and regulators alike. A consolidated tape would educate retail investors more about the best trade prices and quotes which occurred in the market and create competitive pressures so that retail investors cannot be disadvantaged.

(2) Another area is ensuring that the shift away from bilateral over-the-counter (OTC) markets towards central clearing, where it is viable (such as for certain derivatives, repo and securities lending transactions), is done in a way that protects the interest of investors participating in the system to the greatest extent possible. Regarding CCP recovery planning, allocating losses to end-investors through haircutting their margin in a process they often do not choose to enter nor over which they have any control, erodes investor confidence and undermines attempts to build CMU.

Pillar Three: Adopt a company-oriented vision for capital raising

The refreshed CMU agenda should take realistic stock of how companies are turning to markets to raise capital today. While there is a broader public interest served in having a healthy universe of listed companies, there are also good reasons why some companies – in particular, innovative, high growth companies – are choosing to stay private for longer including additional compliance, regulatory and reporting costs.

With this in mind, targeted improvements to the structure of investment vehicles, which help asset owners more efficiently provide capital to companies at different stages of growth, would help grow the investor base. In particular, the ELTIF structure and framework must be further optimised to allow it to play better its role as the vehicle of choice for long-term capital provision. We see three main categories of improvements which would be meaningful changes to the ELTIF framework:

(1) *Structural:* The ELTIF is designed to be an investment vehicle which can provide long-term exposure to a range of long-term assets, but there is often a lack of clarity or too many restrictions in ELTIF investment rules that prevent the structure being used more widely.

(2) *Distribution:* The product was designed to allow retail investors to participate in long-term investment strategies, and indeed we do see appetite and potential for this. However, MiFID (and national) distribution rules do not align with the ELTIF's intended market and a cumbersome cross-border marketing process inhibits the ability to scale products.

(3) *Tax:* Beyond the challenge of navigating different national tax treatments for ELTIF investors, there is added complexity in the treatment of cross-border investments at the fund level. At the fund level, we continue to raise concerns with the tax implications of the OECD Base Erosion and Profit Shifting (BEPS) framework as investment funds that invest in real assets on a cross-border basis will lose some of their tax-neutrality by losing access to tax treaties. We believe an EU-level solution for ELTIFs (at least) would be possible and would make such funds more attractive to end-investors.

Joanna Cound *is Head of Global Public Policy, EMEA, BlackRock and a member of the ICMA Board.*

MiFID II/R and the bond markets: the second year

By Gabriel Callsen

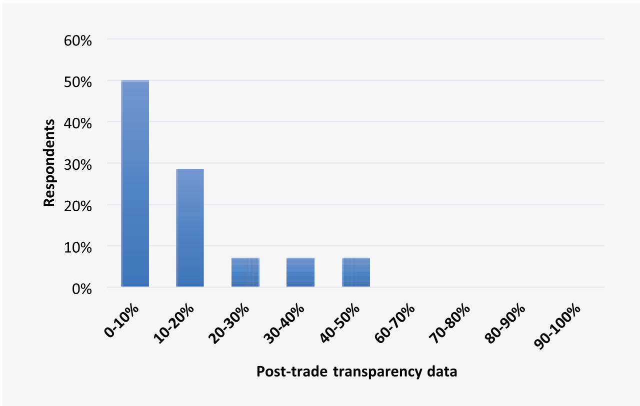
CMU

The second Markets in Financial Instruments Directive (MiFID II) and Regulation (MiFIR) have been in application for two years now. In December 2018, ICMA published its first report, *MiFID II/R and the Bond Markets: the First Year: An Analysis of the Impacts and Challenges of MiFID II/R Implementation Since January 2018,* which revealed that European bond markets and liquidity had not been impacted noticeably in the first 12 months by the new regime. However, it is evident from market participants' feedback[1] that implementation of MiFID II and MiFIR in the European bond markets continued to face a number of challenges in 2019 and has not fully achieved its objectives.

In fixed income primary markets, the impact of MiFID II/R at year-end 2019 is effectively the same as at the end of 2018. Requirements in terms of allocation justification recording and disclosure of underwriting fees do not seem to have generated tangible benefits or interest whilst placing a greater administrative burden on underwriters. However, the product governance and Packaged Retail and Insurance-Based Investment Products (PRIIPs) regimes continue to have significant problematic features that have led to unintended consequences lowering retail investors' participation as well as raising concerns over the fundamental practicability of compliance.

From a secondary markets perspective, electronic trading has further increased across IG, HY, SSA and EM bonds in 2019 while interest in reporting on the quality of transaction execution ("best execution") appears to remain minimal. 15 months after the Systematic Internaliser (SI) regime was introduced, major challenges still persist in identifying whether a counterparty is a SI. However, one of the greatest shortcomings is the continued lack of post-trade transparency in fixed income markets. The results of an ICMA survey suggest that data quality, accessibility of data published through Approved Publication Arrangements (APAs) and usability of data published after deferral periods are key obstacles to creating greater transparency.

Q: In your opinion, what percentage of the publicly available post-trade transparency data under MiFID II/R is usable (ie of sufficient quality and easily accessible)?

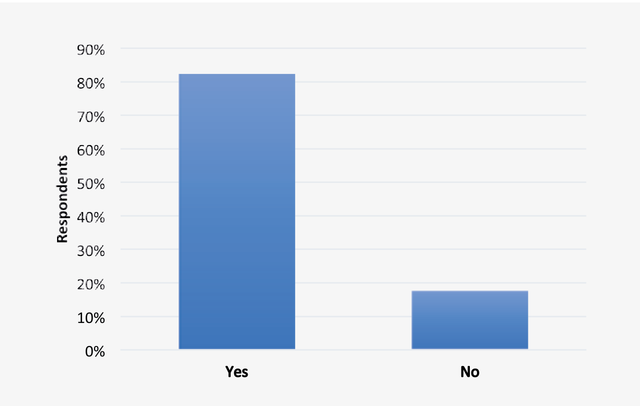


A single, centralised consolidated tape provider (CTP) for bonds in Europe seems to be the preferred solution for aggregating and disseminating post-trade data, according to survey results. Furthermore, market participants reported that a more streamlined approach such as direct reporting of post-trade data to a CTP would be preferable. However, cost is an important consideration and changing regulatory reporting obligations would likely increase costs, at least in the short term. Brexit and the risk of fragmentation is unsurprisingly expected to have a negative impact on an EU27 CT, and the preferred option would be to combine post-trade data from both the EU27

1. In total, 19 responses were received to the secondary markets survey, representing buy-side firms (7), sell-side firms (9), and trading venues or execution services providers (3). Further feedback notably on primary markets and research unbundling is based on discussions in working group and committee meetings as well as informal conversations.

and the UK in a CT post-Brexit. Overall, the extra-territorial impacts of MiFID II/R on market participants seem rather limited, but non-EEA branches of EU firms appear to be impacted adversely while non-EEA trading activity seems to have shifted to non-EU trading venues.

Q: Do you consider that a consolidated tape provider (CTP) would be beneficial for the industry and ensure a level playing field between market participants in terms of market overview and accessibility of transparency data?



In terms of FICC research unbundling, it is evident that research rules have been implemented differently, both within Europe and globally. In the UK, firms have adopted the profit and loss (P&L) approach, Continental European based firms have mostly chosen the research payment account (RPA) model, in the US costs remain bundled, while APAC sees a diverse range of practices. Eventually, performance will determine where assets are allocated, and this, in turn, will determine which system will prevail. Also, regulators have started to review the impact of the investment research rules' implementation in light of its potentially negative impact on SME research. At the same time, the new rules have given rise to research management systems (RMS), which are an increasingly important tool in institutional investment management.

In summary, implementation of MiFID II/R is a continuing process and ICMA will continue to work with its diverse membership and engage with EU authorities and national competent authorities to help achieve the desired regulatory outcomes while maintaining resilient and efficient markets. The full report is available on ICMA's website.

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One of the greatest shortcomings is the continued lack of post-trade transparency in fixed income markets.

CSDR impact study on mandatory buy-ins

By Andy Hill

CMU

Background

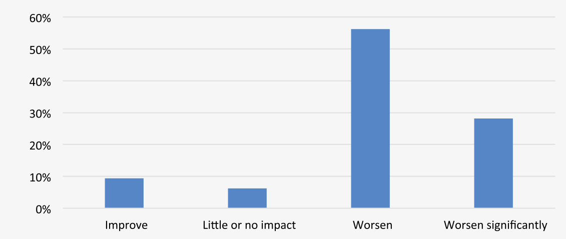
In 2015, mainly in response to concerns raised by sell-side members, ICMA undertook an impact study of the projected CSDR mandatory buy-in provisions on European bond markets.[1] A controversial piece of market regulation buried in legislation focused on settlement systems, the CSDR buy-in framework is a radical reinterpretation of how contractual buy-ins work in the non-cleared securities markets: legally, structurally, and potentially economically. Most significantly, the regulatory provisions would increase the market risk of liquidity providers considerably.

In September 2019, ICMA launched a second impact study. Similar to the previous study, this set out to ascertain the potential impacts on liquidity and pricing across a range of fixed income sub-classes. This time, the surveys also focused on three main constituencies: sell-side market-makers, buy-sides, and repo and securities lending desks.[2] It also sought to establish market preparedness and expectations, as well as assessing potential modifications intended to lessen the undesirable consequences of the buy-in framework. The final report of the impact study was published in November 2019.

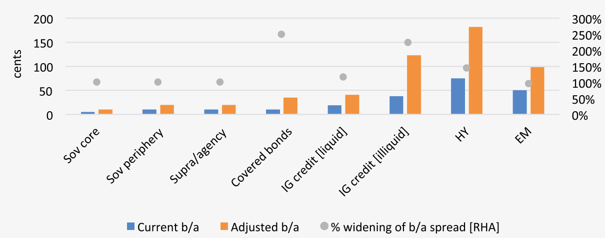
Market impact

Overall, the mandatory buy-in regime is expected to have significant negative impacts for bond market liquidity and efficiency. In terms of price impacts of the Regulation, bid-ask spreads of all bond sub-classes are expected to more than double, with covered bonds and illiquid IG credit seeing the biggest impact. In absolute price terms, the impact is most notable at the lower end of the credit spectrum, with significant increases for emerging market, high yield, and illiquid IG credit bonds. The new buy-in regime is further expected to impact the capacity of market-makers to show offers across all bond sub-classes, with core sovereign markets the least affected. Again, it is the lower end of the credit spectrum that is most impacted, in particular illiquid IG credit and high yield.

Expected impact on market efficiency and liquidity



Impact on bid-ask spreads



1. ICMA Impact Study for CSDR Mandatory Buy-ins (2015)

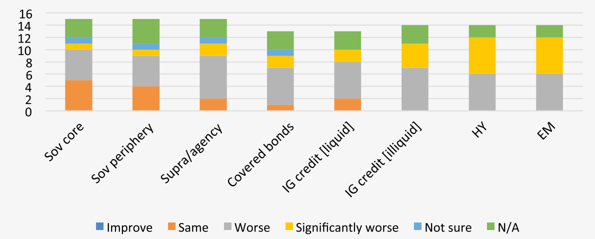
2. In total, there were 44 responses to the survey, representing buy-side firms (16), sell-side firms (16), and repo and securities lending desks (12).

The mandatory buy-in regime is expected to have significant negative impacts for bond market liquidity and efficiency.

Buy-side expectations

Buy-side expectations for the impact on pricing are largely consistent with the indications of price adjustment from sell sides. While they expect a general worsening of offer-side pricing across all sub-classes, there is a realisation that the biggest impact will be at the lower end of the credit spectrum.

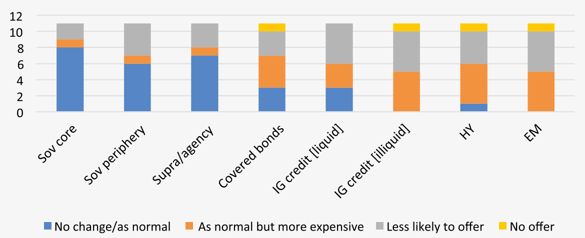
Expected impact to offer-side pricing



Repo and securities lending

The survey responses suggest that, for the most part, lending and repo activity will continue as normal for SSAs. For other sub-classes of bonds, however, the indication is that borrowing securities will become both more expensive and more difficult.

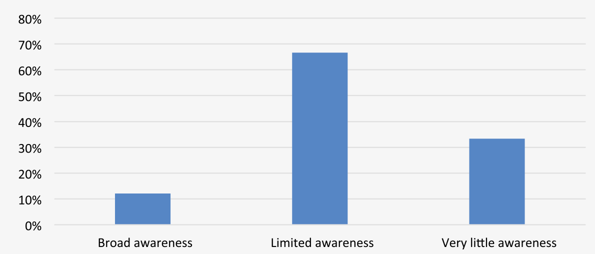
Expected impact on lending securities



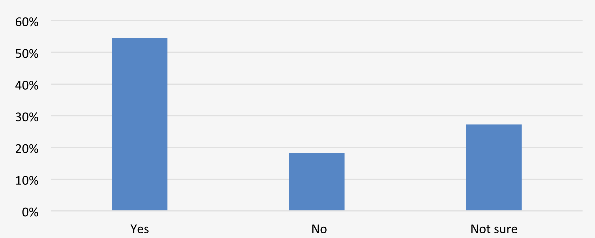
Preparedness

More than half of respondent firms have plans to adapt their operational processes as well as their approaches to trading and risk management, with repo and securities lending businesses leading the field. However, the general view across all constituents is that there is limited or little market awareness of the regulatory requirements and likely impacts.

Market awareness



Plans to adapt risk management and trading



Conclusion

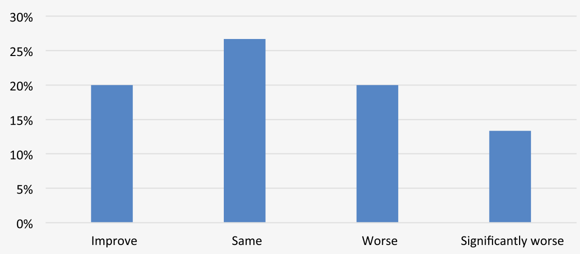
The survey results support the broad market view that the CSDR mandatory buy-in regime is likely to have a significant impact on European bond market pricing and liquidity across all bond sub-classes, but most acutely at the less liquid end of the credit spectrum. There is also a wide perception of a general lack of awareness of the regulatory requirements and likely impacts across the market.

While many respondent firms are beginning to adapt both their operational processes and trading and risk management approaches, there are still a number of uncertainties that would benefit from clarification, such as the ability to solve for the payment asymmetry, the possibility of a pass-on mechanism, and the scope of application to SFTs.

However, what the study highlights quite clearly is that, to avoid the potentially significant negative impacts on bond market liquidity and pricing, the regulators should consider more intrinsic modifications to the Regulation, such as applying a much longer extension period, or exempting less liquid (or all) bond asset classes.

Finally, if the intention of the CSDR mandatory buy-in regime is to improve investor protection, there is little confidence or expectation among respondents that it will achieve this objective.

Expected impact on investor protection



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An overview of EBRD's pioneering green bond programme *by Isabelle Laurent, EBRD*

SF When the EBRD issued its first green bonds in 2010 to fund its Environmental Sustainability Bond programme, there were many aspects that were innovative, especially in seeking to address a broader range of environmental concerns than solely climate change mitigation.

EBRD's green bond framework was drafted to allow for refinancing of existing projects in recognition both of the long disbursement time for such projects (typically over three years) and the long tenors (averaging over ten years), but including only projects in which at least 90% of the monies were directed towards the environmental objective. Despite the potential to include several of the ten project categories under the subsequent ICMA-supported Green Bond Principles (GBP), over 75% of the proceeds were focused on EBRD's climate mitigation investments, and most especially those that could operate in a low carbon environment today.

Collaborating with the Climate Bond Initiative on their Climate Resilience Principles (CRP), launched in September 2019 to provide clarity on potential resilience investments, encouraged EBRD to identify climate resilience projects that could be funded by green bonds issued in conformity with both the GBP and the CRP. EBRD established a new framework to focus primarily on climate-resilient infrastructure; climate-resilient commercial operations; and climate-resilient agriculture and ecological systems.

Besides the singular environmental objective of the 65 projects under EBRD's newly established Climate Resilience Portfolio, the framework allows for less than 90% of the monies to go to making the asset resilient, as long as the remaining monies are disbursed in consistency with robust climate change mitigation and adaptation requirements.

EBRD's third portfolio for Green Bond issuance was simultaneously set-up focused on decarbonisation and improved resource efficiency projects in those key sectors of the economy that are today highly dependent on fossil fuels and which will likely remain key to achieving the transition towards net zero carbon emissions. Projects funded through EBRD's Green Transition Bonds include significant resource improvements in the chemical, cement and steel production; food production; in agribusiness and sustainable land use; in transport systems; and in the construction and renovation of buildings.

It is important to ensure that transition projects avoid locking in a carbon intensive asset or process for the longer term, thereby excluding new fossil fuel electricity generation. Where, however, significant CO_2 reductions could be made by switching from old and inefficient oil and coal facilities to gas, these were deemed compatible with green transition if the project employs the best available technology, and there is no feasible alternative for that specific location.

The importance placed by the GBP on framing the environmental objectives of projects to be financed by green bonds "within the context of the issuer's overarching objectives, strategy, policy and/or processes relating to environmental sustainability" is especially relevant to Green Transition Bonds under EBRD's framework. In high emitting and resource intensive economic sectors, even the best projects can only be credibly deemed "transitional" if the relevant borrower commits to implement measures to improve their organisation's climate governance and sustainability. Where an additional portion of the loan includes operating expenditures, the total project may only be included where it is clear that the borrower is making changes at an organisational level in consistency with the project's transition objectives, and where this is reflected in covenants that form part of the project documentation.

Underlining the primary objective of the projects to be funded by Green Bonds through different frameworks serves to improve the transparency of the market and has further enhanced EBRD's dialogue with investors. And it is this heightened transparency and dialogue between green bond market participants, which is at the core of the GBP – so ably promoted globally by ICMA – that is critical to the market fully supporting vital changes to the real economy.

Isabelle Laurent *is Deputy Treasurer & Head of Funding at the EBRD and has been a GBP Excom member since 2015.*

Summary of practical initiatives by ICMA

The practical initiatives on which ICMA has been engaged over the past quarter, with – and on behalf of – members, include the following:

Transition to risk-free rates

1 ICMA continues to participate in the RFR Working Groups in the UK, the euro area and Switzerland; and ICMA is chairing the Bond Market Sub-Group in the UK, working with the FCA and Bank of England, and is in regular contact with the equivalent group in the US Alternative Reference Rates Committee (ARRC), which is working with the Federal Reserve. In the ICMA Quarterly Report for the First Quarter of 2020, the Quarterly Assessment is on *The Transition from LIBOR to Risk-Free Rates: Legacy Bonds.* There is also a feature article on global developments relating to the transition to risk-free rates.

2 ICMA responded in December 2019 to the European Commission's consultation on the EU Benchmarks Regulation.

Primary markets

3 *Public sector issuers:* The Public Sector Issuer Forum (PSIF) met at the World Bank in Washington on 17 October to discuss the transition to risk-free rates, particularly in the US, introduced by the Federal Reserve and the World Bank, cyber-security and Brexit.

4 *MAR:* ICMA responded on 29 November to an ESMA consultation on MAR.

5 *Prospectus Regulation:* ICMA is working with members on implementation of the new Prospectus Regulation regime (including consequential revisions to the ICMA Primary Market Handbook) and considering potential disclosure requirements related to ESG.

6 *MiFID II/R:* ICMA has been working with members on refining implementation of the allocation justification recording requirements and on German Ministry of Finance findings relating to a potential review of the product governance regime.

7 *PRIIPs:* ICMA is working with members on the implications of an ESAs' statement on scope and on a high-level response to the ESAs' consultation on Level 2 KID content.

8 *Deal announcements and new issue processes:* ICMA is facilitating industry discussions among buy-side and sell-side market participants on the format of deal announcements and on new issue processes.

9 *Post-trade:* ICMA is working on the primary market implications of various emerging post-trade initiatives, including: EDDI; the ECB AMI-SeCo Collateral Management Harmonisation Task Force consultation on corporate action harmonisation; and potential reforms to the ICSD syndicated closing process following CSDR implementation.

10 *Primary markets technology mapping directory:* ICMA has reviewed its mapping of existing and emerging platforms and technology solutions in primary markets, which was initially launched in December 2018. The new version was published on 18 September 2019. The purpose is to help inform ICMA members and thereby create greater transparency.

11 *Primary Market Forum:* ICMA held its annual Primary Market Forum in London on 14 November, hosted by The London Stock Exchange. The event attracted over 120 participants and comprised panels on capital market developments and keynote speeches on FinTech and diversity, inclusion and well-being.

Secondary markets

12 *ICMA SMR&R:* ICMA is consulting members on the impact of MiFID II/R and other proposed new EU regulations on the ICMA Secondary Market Rules & Recommendations (SMR&R), and has established a dedicated working group to review the ICMA SMR&R. In particular, the working group will look to revise the ICMA buy-in rules in light of the new CSDR requirements.

13 *CSDR mandatory buy-ins:* ICMA, through its CSDR Settlement Discipline (CSDR-SD) Working Group, remains highly focused on the implementation of the mandatory buy-in framework, which is scheduled to come into force in September 2020, but is likely to be delayed for technical reasons. The CSDR-SD Working Group has two priorities: (i) addressing practical implementation challenges, both for cash bonds and repo; and (ii) advocacy and raising awareness.

14 *Corporate bond secondary market:* ICMA is nearing completion of its research for the third ICMA study into the state and evolution of the European IG corporate bond secondary market. Intended to update on the seminal 2016 report, the new study seeks to address three key questions: (i) What is the current state and expected course for market liquidity? (ii) How is the structure of the market evolving? (iii) What are the expectations for future market developments? ICMA plans to publish the new report in Q1 2020.

15 *MiFID II/R:* Following its review of MiFID II/R at the end of 2018, ICMA published a second annual review of MiFID II/R in December 2019.

16 *MiFID II/R data quality:* ICMA has established a MiFID II/R Data Quality Task Force which has identified key challenges and provided practical solutions relating to MiFID II/R post-trade data. The objective of the Task Force is to work with ESMA and the European Commission in improving the existing data structures and systems in a cost-effective way.

17 *An EU bond consolidated tape:* In response to a request from the European Commission, ICMA submitted an interim report to the Commission on 16 December on an EU bond consolidated tape.

18 *Brexit Technical Working Group:* ICMA has established a technical working group to focus on the practicalities of Brexit relating to the secondary bond and repo markets in the EU27 and the UK.

19 *ICMA Secondary Markets Newsletter:* ICMA has launched a new *Secondary Markets Update* which provides a quick summary of ICMA's current initiatives and workstreams, pertinent news and regulatory updates affecting the secondary bond markets. It is to be published on a bi-monthly basis.

20 *ETP mapping directory:* ICMA has updated its mapping directory of Electronic Trading Platforms (ETPs). The directory now lists a total of 43 electronic execution venues, Order Management Systems (OMS) and information networks. It is intended to help market participants understand what execution and non-execution venues are available for cash bonds. The revised mapping is available on ICMA's website.

Repo and collateral markets

21 *SFTR implementation:* Helping members to implement the extensive reporting requirements under the EU's SFT Regulation (SFTR) continues to be a key priority for ICMA and its members, who are heavily engaged in the ERCC's dedicated SFTR Task Force. This brings together representatives from over 120 firms across the whole market spectrum to coordinate the industry's implementation effort in relation to repos and buy/sell-backs.

22 *Common Domain Model:* ICMA is cooperating with ISDA to extend the development of the Common Domain Model (CDM) to include repo and, by extension, outright bond transactions: a single, common digital representation of securities trade events and lifecycles intended to enhance standardisation and facilitate interoperability across firms and platforms. The development of the CDM for all financial markets and securities will be critical in creating cross-industry efficiencies, while easing the development and adaptation of new technologies.

23 *ECB AMI-SeCo:* The ERCC is represented on the ECB's Advisory Group on Market Infrastructure for Securities and Collateral (AMI-SeCo) and is playing an active role on its Collateral Management Harmonisation Task Force (CMH-TF).

24 *Balance sheet netting and T2S:* The ERCC has raised concerns about the possibilities for balance sheet netting in T2S and is coordinating an industry discussion on this topic with the relevant accountancy experts. In this context, ICMA hosted a meeting on 10 September between ERCC members, experts from the major accountancy firms and T2S experts from the ECB in order to lead the discussion towards a positive conclusion.

25 *Basel III implementation:* The ERCC remains focused on the implementation of Basel III measures with respect to SFTs, in particular the Leverage Ratio, the Liquidity Coverage Ratio, the Net Stable Funding Ratio, and minimum haircut floors. The ERCC submitted its response to the European Commission's consultation document on *Implementing the Final Basel III Measures in the EU* on 2 January.

26 *FinTech mapping for repo and cash bonds:* The FinTech Working Group of the ERCC has conducted a review of the FinTech mapping directory for repo and cash bond operations to ensure it is up-to-date. The revised mapping is available on ICMA's website.

Sustainability markets

27 *TEG:* Following the publication in March 2018 of the European Commission's Action Plan on Sustainable Finance, the Technical Working Group on Sustainable Finance (TEG) was established in June 2018. ICMA, with the support of the GBP SBP Excom, was nominated on the TEG, which has held monthly working group and plenary meetings since its inception. On 18 June 2019, the TEG published reports and guidelines relating to its four key deliverables and ICMA has produced an overview and comments on these reports.

28 *EU Taxonomy:* On 18 December 2019, the European Council and the European Parliament reached a political agreement on the Taxonomy Regulation. The Regulation will introduce a complex classification system of sustainable activities based on contributions to environmental objectives and technical criteria, as well as wider social and sustainability factors. It also recognises transition and enabling activities. ICMA has published an overview and comments on the text of the agreement.

Asset management

29 *Fund liquidity:* The ICMA Asset Management and Investors Council (AMIC) is working with EFAMA on updating their joint fund liquidity report. AMIC and EFAMA members are: (i) calling for a stronger enforcement of the current rules rather than new provisions; (ii) recommending that liquidity management tools should be made available across all EU jurisdictions; (iii) asking for data to be made available better to understand investors' behaviour and redemption patterns; and (iv) flagging the impact of monetary easing and market making rules on market liquidity.

30 *Sustainable Finance Working Group:* At the request of the AMIC Executive Committee, the AMIC Sustainable Finance Contact Group has been converted into a Working Group, which met for the first time on 3 December. This group will provide a dedicated platform for AMIC members to discuss the trends and development of the ESG market and relevant regulatory files, such as the EU Ecolabel for investment funds, ESG disclosures, climate benchmarks, and integration of sustainability risks in UCITS and AIFMD.

31 *AMIC Conference:* The latest AMIC Conference was hosted by BlackRock in London on 27 November. Its agenda featured Fabrice Demarigny, Chair of the Next CMU High-Level Working Group, as a keynote speaker on the topic of CMU, followed by panel discussions led by industry practitioners on the development of the STS securitisation market; the pension gap, PEPP and the effect of negative interest rates; and the possibility of an EU Ecolabel for funds. The next AMIC Conference is planned for March 2020.

FinTech in capital markets

32 *FinTech meetings with regulators:* ICMA held meetings and calls with the FCA on 7 October and 4 November respectively, and met the FSB and BIS on 20 November to discuss FinTech and related legislative and regulatory developments.

33 *ECB FinTech Task Force:* ICMA, through the ERCC Ops FinTech Working Group, continues to be represented on the ECB's Harmonisation Steering Group's FinTech Task Force, a sub-group of the AMI-SeCo, following the renewal of its mandate. ICMA contributes, for example, to the mapping exercise of post-trade technology solutions, as well as discussions on tokenisation of securities.

34 *IOSCO FinTech Network:* ICMA, an affiliate member of IOSCO, is represented on the IOSCO FinTech Network, and continues to participate in the workstream on distributed ledger technology (DLT). The purpose of the network is to share information and practices with respect to FinTech in an informal manner.

35 *ICMA Regional FinTech conference:* On 9 October in Paris, ICMA's Regional Committee for France and Monaco held a conference entitled *The Impact of New Technologies on Fixed Income Professionals – What Is the New Paradigm?* The event was hosted by the Banque de France and brought together over 100 participants across the international debt capital markets as well as regulators.

Other meetings with central banks and regulators

36 *ICMA Regulatory Policy Committee (RPC):* Ugo Bassi, Head of Directorate C, Financial Markets, DG FISMA, European Commission, joined the ICMA RPC meeting in Brussels on 12 December for a discussion.

37 *Other official groups:* ICMA continues to be represented, through Martin Scheck, on the ECB Bond Market Contact Group and on the ESMA Securities and Markets Stakeholder Group; through Nicholas Pfaff on the European Commission Technical Expert Group on Sustainable Finance; through Charlotte Bellamy on the Consultative Working Group on ESMA's Corporate Finance Committee; and through Gabriel Callsen on the ECB AMI-SeCo Harmonisation Steering Group Task Force on FinTech Innovation in Securities Post-Trading (FinTech-TF).

38 An updated draft of the ICMA regulatory grid is available on a password-protected webpage on the ICMA website.

ICMA's approach to Brexit

Following the agreement reached between the EU27 and the UK on 17 October 2019 and the re-election of the Conservative Government in the UK on 12 December, the UK is expected to leave the EU on 31 January 2020, once the agreement has been ratified by Parliament in the UK and the European Parliament. The EU Single Market will become two separate markets when passporting rights cease at the end of the transition period at the end of 2020.

By historic standards, this transition period of just under one year is a very short interval in which to negotiate and ratify a trade agreement between the EU27 and the UK. There would be an opportunity for the EU27 and the UK to agree by June 2020 to extend the transition period for a further two years until the end of 2022. But the Conservative Government ruled out this option in its election manifesto and is writing this commitment into law. So there is a risk that the UK will leave at the end of the transition period without a trade deal, or with a basic trade deal which does not sufficiently cover financial services.

ICMA's approach to Brexit has been to focus on its potential impact on international capital markets, particularly the need to address and avoid cliff-edge risks which arise when passporting rights between the EU27 and the UK cease; and the scope for regulatory equivalence between the EU27 and the UK after Brexit. A detailed assessment of both these issues was included in the ICMA Quarterly Report for the Fourth Quarter of 2019 under the heading, *Brexit: Can Capital Market Fragmentation Be Avoided?*

In addition:

(i) ICMA is not lobbying for any particular financial centre; ICMA's members are based in London, the EU27 and more broadly;

(ii) ICMA has been discussing capital market preparations for Brexit with members through its main ICMA Market Practice and Regulatory Policy Committees and reporting to the ICMA Board;

(iii) ICMA is keeping in contact with the authorities in the UK, the EU27 and the euro area;

(iv) ICMA is cooperating with other trade associations by sharing information, wherever possible:

(v) ICMA is keeping members up-to-date on Brexit by giving them regular assessments through the ICMA Quarterly Report and conference calls;

(vi) ICMA has posted on its website for members an ICMA Brexit FAQ, focusing on ICMA's own documentation; and is monitoring the need to update its documentation and standard language; and

(vii) ICMA is keeping its Brexit webpage up-to-date, both with its own work, and also with electronic links to key documents published by the authorities in the EU27 and the UK, and with links to the webpages of law firms and others.

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Primary Markets

by Ruari Ewing and Charlotte Bellamy

CMU The EU Prospectus Regulation: six months in

The impact of the new EU Prospectus Regulation, which replaced the previous Prospectus Directive in full in July 2019, is likely to be felt by many international bond issuers for the first time as we enter 2020. This is because most international bond issuance takes place under debt issuance programmes, the prospectuses for which (known as base prospectuses) only need to be updated annually. Many issuers will be updating their base prospectus under the new regime for the first time in H1 2020. With this in mind, we set out below a recap of the key changes introduced under the new regime that impact international bond markets.

General

The new EU Prospectus Regulation was developed as part of the European Commission's Capital Markets Union initiative. The legislative process started in 2015 with a review of the previous EU prospectus regime, the Prospectus Directive. The Commission stated that the purpose of its review was to "reform and reshape the current prospectus regime in order to make it easier for companies to raise capital throughout the EU and to lower the associated costs, while maintaining effective levels of consumer and investor protection." With this background, market participants wondered if there would be radical changes to the incumbent regime.

ICMA engaged heavily in the legislative process (as detailed in previous editions of this ICMA Quarterly Report), including on topics such as the retention of the alleviated disclosure regime for bonds with a minimum denomination of at least €100,000 which, helpfully, was kept in the end.

The ultimate outcome is that the radical changes that many bond market participants hoped for or feared (depending on the subject matter) did not materialise; and, generally, there have been limited practical changes for mainstream bond market participants working under the new regime. This is viewed as a good thing by many bond market participants, on the basis that they were familiar with the Prospectus Directive regime and it worked reasonably well in practice.

Structural changes

The new Regulation did introduce some structural changes, largely adding new options or flexibility to the infrastructure of the regime rather than changing or restricting the options that issuers had under the previous Prospectus Directive regime. While some of these might be relevant for bond issuers, the expectation is that the overall impact of these changes is likely to be marginal.

- *Qualified investors only:* One such structural change was the extension of the "wholesale" disclosure regime and exemption from the requirement to prepare a prospectus summary (which was previously only available in the case of bonds with a minimum denomination of €100,000 or more) to bonds which are to be admitted to trading on a regulated market, or a specific segment thereof, to which only qualified investors can have access. ICMA had supported this approach during the legislative process on the basis that it could be a useful way to allow issuers to issue low denomination bonds to qualified investors without needing to prepare onerous "retail" disclosure under the Prospectus Regulation. ICMA is aware of two "qualified investor only" regulated markets that have been established since the Prospectus Regulation was finalised. So far, we understand there has been limited use of these new markets, and many issuers have chosen to continue to issue their securities in high minimum denominations. There could be a number of reasons for this, some of which may be linked to considerations arising under other regulatory regimes such as the MiFID II product governance regime and the PRIIPs Regulation, along with other (non-regulatory) reasons for issuers not wishing or needing to issue low denomination securities.

- *Simplified disclosure regime for secondary issuance:* Another new structural change that could be relevant to ICMA members is the concept of simplified disclosure for "secondary issuances". The simplified disclosure regime is available to, among others, bond issuers where the issuer's shares have been admitted to trading on a regulated market or SME growth market continuously for the last 18 months or more. The level of take-up for this new regime remains to be seen. The initial view of some ICMA members is that some bond issuers may not be convinced that the alleviations available through the secondary disclosure regime outweigh the other requirements of the regime, most notably the requirement for a summary of the information disclosed under MAR over the last 12 months which is relevant as at the date of the prospectus.

Other "structural" changes to the regime are also generally viewed as unlikely to impact on current market practice for most bond issuers. For example, ICMA members have so far not expressed a widespread degree of interest in adopting the new "universal registration document", building on the French "*document de référence*". Similarly, the EU Growth Prospectus is aimed primarily at SMEs and so is unlikely to be relevant or available to many ICMA sell-side members.

Risk factors

Perhaps the main area where bond market participants will notice a change under the new Prospectus Regulation is risk factor disclosure. This was a key issue for legislators in formulating the new regime, amidst concerns that previous risk factor disclosure could be overly lengthy and difficult for investors to navigate. A new provision was introduced (Prospectus Regulation Article 16), which requires issuers to limit risk factor disclosure to those risks that are specific to the issuer and/or the securities and which are material for an informed investment decision, as corroborated by the content of the prospectus. Issuers are also required to assess the materiality of risk factors and have the option (but are not compelled) to disclose that assessment by using a qualitative scale of low, medium or high. Risk factors must also be categorised depending on their nature and the most material risk factors in each category must be mentioned first. ESMA has issued *Guidelines on Risk Factors under the Prospectus Regulation* designed to assist competent authorities in their review of risk factors.

The precise implications of these new requirements are likely to become clearer as competent authorities start to review and approve more prospectuses in the coming months. One thing, however, seems to be clear: risk factor disclosure is a key area of focus for authorities and simply following previous practice is unlikely to be an option for many issuers.

Advertisements

Another aspect that impacts ICMA members is the newly widened definition of "advertisement", which was amended from an "announcement" under the Prospectus Directive to a "communication" under the new Prospectus Regulation. While the rules relating to advertisements are not radically different from those under the Prospectus Directive regime (particularly in the context of exempt – or "wholesale" – public offers), there are some new requirements such as the need to include hyperlinks to the prospectus and final terms or to the webpage where the prospectus will be published. In addition, the newly broadened scope means that bond underwriters and others have needed to consider which communications fall within the newly widened regime and which do not. ICMA facilitated discussions among members on this topic when the new Prospectus Regulation was introduced and market practice in this area appears to be bedding down.

Summaries

The summary regime under the previous Prospectus Directive was widely criticised, primarily due to its rigidity and the negative impact that it had on the helpfulness of prospectus summaries for retail investors. Many market participants were pleased to see that the summary regime was overhauled under the Prospectus Regulation, with the new requirements being set out at Level 1. There were some concerns from ICMA members with the new regime, such as the limit on the number of risk factors that can be included in the summary. It is also worth noting that the new regime makes it clear that it is *not* possible to include a summary in a base prospectus, and this has been confirmed by ESMA in its *Q&A on Prospectuses*. It remains to be seen whether this will impact upon issuers seeking to draw up a summary at the time of a drawdown under a programme. However, as noted above, the majority of international bond issuers issue securities with a minimum denomination of €100,000 or more and, helpfully, the exemption from the requirement to prepare a summary for prospectuses relating to such securities was retained in the Prospectus Regulation. That exemption now also applies in the case of prospectuses for securities that will be traded on a "qualified investor only" market or market segment. As such, the prospectus summary requirements are unlikely to be applicable to the majority of international bond issuance for the reasons noted above.

Other changes

The new regime introduced some other small, but nevertheless helpful, changes for bond market participants.

- *Withdrawal rights:* Among these was a confirmation by ESMA in its *Final Report on Draft RTS under the new Prospectus Regulation* that withdrawal rights do not arise in the context of exempt offers of wholesale securities being admitted to trading. This had been a source of much debate when the Prospectus Directive was revised in 2012.
- *Taxation disclosure:* Another change that was considered to be helpful by ICMA members was a confirmation in Recital 47 of the Prospectus Regulation that prospectuses need only contain a warning that the tax laws of the investors' and issuer's Member State might have an impact on the income received from the securities. Detailed tax disclosure relating to the countries where an offer may be made or where admission to trading may be sought (which, for a passported prospectus could be several Member States) is no longer required.

Outstanding areas of concern

There are currently a relatively small number of areas which ICMA members have identified as being potentially problematic or unclear in practice for the international vanilla bond market, such as the categorisation of certain disclosure requirements in the Level 2 delegated regulation, which impacts upon whether the information can be provided in final terms or whether it needs to be provided in the base prospectus. There are reportedly also some concerns in other markets (eg in relation to which Level 2 disclosure requirements apply in the context of convertible bonds and how certain Level 2 disclosure requirements can be complied with in the context of structured products referencing non-EEA ISINs). Further concerns could arise as more prospectuses are submitted for review under the new regime. ICMA will continue to engage with members and the authorities on any such issues.

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Other issues impacting prospectus disclosure

In addition to the new Prospectus Regulation regime itself, there are a handful of other initiatives with the potential to impact upon prospectus disclosure and practice.

- *Brexit:* The UK's withdrawal from the EU will impact upon the ability of issuers to passport their prospectuses between the EU27 and the UK when passporting rights cease. ICMA has published Q&A on this topic for ICMA members.
- *ESG disclosure:* ICMA is also monitoring developments in the area of ESG disclosure, including developments connected with the proposal in the *European Commission Action Plan on Financing Sustainable Growth* to specify prospectus content for green bond issuances. In this regard, it was interesting to see a joint *Position Paper on Green / Social / Sustainable Bonds* published by the AFM and AMF in April 2019 suggesting that a "full prospectus Annex" under Level 2 of the Prospectus Regulation is not necessary, and recommending an alternative approach under which (i) the issuer would be solely responsible for qualifying its bond issuance as green, social or sustainable; and (ii) should it decide to qualify its issuance as such, the issuer would be required to provide additional information in the "use of proceeds" section of the prospectus, notably whether it intends to comply with green bond voluntary standards (such as ICMA's *Green Bond Principles* or the Climate Bond Initiative's Climate Bond Standards), to publish a report on the use of the green bond proceeds and to mandate a third party verification.

Many issuers will be updating their base prospectus under the new regime for the first time in H1 2020.

- *ESMA Q&A on Prospectuses and National Competent Authority Guidance on the Prospectus Regulation:* These publications can also impact upon market practice in the area of prospectus disclosure. ICMA is not currently aware of any concerns with the most recently published *ESMA Q&A on Prospectuses*. In relation to national competent authority guidance, BaFin published a guidance note (available in German) on 10 September 2019 setting out the criteria it intends to apply when scrutinising prospectuses for compliance with the requirements of "comprehensibility" under the Prospectus Regulation regime. It will be interesting to see if other national competent authorities publish similar guidance on this (or other) topics and, if so, the impact this could have upon prospectus disclosure across Europe (noting that a core purpose of the Prospectus Regulation regime is to harmonise prospectus disclosure).
- *Review of the ESAs:* As previously reported in this Quarterly Report (eg in the Q4 2017 edition), during the review of the European Supervisory Authorities (EBA, EIOPA and ESMA), the European Commission proposed the transfer of powers to approve certain types of prospectus from national regulators to ESMA. ICMA and others raised concerns that this could negatively impact upon the efficiency (in terms of speed, predictability and cost) of the current prospectus approval process with national regulators. This proposal was not taken forward in the final legislative agreement among the European Parliament, Council and Commission and so, for the time being at least, the *status quo* in relation to prospectus approval with national competent authorities (rather than ESMA) is expected to endure.

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The new Swiss prospectus regime: a practical guide

On 1 January 2020, the new Swiss Financial Services Act "FinSA" (Finanzdienstleistungsgesetz "FIDLEG" / Loi fédérale sur les services financiers "LSFin") came into effect, together with its subsidiary implementing ordinance "FinSO" (Finanzdienstleistungsverordnung "FIDLEV" / Ordonnance sur les services financiers "OSFin") that was approved on 6 November 2019.

This new regime, which constitutes a major overhaul of the Swiss prospectus requirements, modernises the Swiss legal framework for capital market issuances, amongst other things revising the prospectus requirements for Swiss market issuers and underwriters. The current arrangements around the Swiss vanilla debt market provide for flexible access and allow many issuers to enter the market within a short time frame and the new arrangements under FinSA preserve this flexibility in many instances. Four alternatives are available to issuers (see Homburger's October 2019 briefing for further detail) and the choice depends to a large extent on the current status of the issuer in terms of existing issuance programmes, listings and disclosure obligations.

Ex-ante approval: Before debt securities can be publicly offered in Switzerland or admitted to trading on a Swiss trading venue, a prospectus (in English or one of Switzerland's official languages) must be approved by a review body licensed by the Swiss Financial Market Supervisory Authority (FINMA) and published. Draft prospectuses need to be submitted ten calendar days in advance for repeat issuers (20 days for first-time issuers) and can incorporate a wide range of existing documents by reference. It is envisaged that this route is likely to be used for first time or infrequent issuers and is analogous to the current situation where such issuers generally present a preliminary prospectus prior to launch.

Ex-post approval: This alternative preserves the speed to market enjoyed by many issuers in the Swiss market currently. Where (notably) a debt securities issuer receives a confirmation (the Confirmation) from an underwriting Swiss bank or securities firm that that the most important information about it, any guarantor and the debt securities is publicly available when the public offer begins, then the draft prospectus need *only* be submitted for approval within two months thereafter. (In practice the unapproved final prospectus is likely to be published prior to settlement, with submission for approval following thereafter.)

In providing for this Confirmation, FinSA in effect tasks the relevant Swiss bank or securities firm as the gatekeeper for Swiss investor protection for this particular issue of debt securities. In this respect and as a practical approach to being able to issue the Confirmation, it is envisaged that the Swiss bank or securities firm (most likely to be the member of the underwriting group which is undertaking the documentation for the issue and in parallel to usual due diligence procedures) will request a written confirmation from the issuer (and any guarantor) to evidence the basis on which the Swiss bank or securities firm was satisfied that the most important information is indeed publicly available at the time of launch.

It is expected that this route will be most appropriate for issuers that already have debt or equity securities listed at the time of launch on a stock exchange which meets the requirements of the Swiss review body.

Filing / automatic approval: A further alternative, for prospectuses already approved by a recognised non-Swiss regulator (expected to be *inter alia* from the EU and the US)

The new regime, which constitutes a major overhaul of the Swiss prospectus requirements, modernises the Swiss legal framework for capital market issuances.

and in English or one of Switzerland's official languages, is to just file the prospectus electronically within either of the above timelines (subject, in the *ex-post* context, to a Confirmation having been delivered).

Grace period / preceding regime: The new prospectus regime is subject to a grace period until the end of September 2020 (or, if later, six months from when the first review body receives its FINMA licence). Until this date, prospectus content can continue to comply with the preceding Swiss regime. (However, once the first review body is licensed under the new regime, it is likely that many issuers will adopt the new practices irrespective of the grace period.)

ICMA has had extensive discussions with the Swiss underwriting and legal community during the formulation of these practices and welcomes the suggested practices which provide a practical and straightforward route to maintaining the flexibility and speed to market of the Swiss market whilst ensuring that investor protection is maintained and satisfy the new FinSA regime.

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The ESMA market abuse consultation

CMU

On 29 November 2019, ICMA responded to ESMA's 3 October 2019 consultation on a review of the EU's Market Abuse Regulation (MAR).

Generally, ICMA's response noted: (i) the need for further consultation on any specific proposals not in this consultation; (ii) the cost of any regulatory change needing to be weighed against its benefit; (iii) MAR's full effect on risk management tools (such as pre-sounding and stabilisation) having been dampened so far by ongoing bull market conditions; (iv) the need for a real-time list of MAR Article 2.1(a)-(c) securities following MAR's extension to MTFs/OTFs; (v) there having been no ESMA feedback on ICMA's 2014 proposed improvements to the stabilisation safe harbour; (vi) ICMA having previously supported a buy-back safe harbour extension to DCM; and (vii) the potential value in ESMA's Market Integrity Standing Committee having its own consultative working group.

Regarding inside information, the response noted: (i) MAR's definition to be more than wide enough; (ii) illiquid markets are anyway more sensitive in this respect; (iii) pre-hedging dynamics and that such trading activity is sufficiently regulated under MiFID II (with any actually abusive conduct already prohibited under MAR); (iv) that it is unclear how securitisation SPVs could operate prescriptive systems and controls.

Regarding pre-sounding, the response noted: (i) the current Article 11 sounding provisions are not entirely obligatory (with the granular sounding procedures relevant only as a condition to safe harbour application); (ii) only a change to MAR Article 11 itself can make the granular sounding procedures obligatory; (iii) the disproportionate burden arising from such change (reduced sounding and so issuance); (iv) there being no proportionate justification for such change (including in terms of audit trail benefit); (v) safe harbours are intrinsically voluntary; (vi) there is no need for further *"full protection"* confirmation; (vi) no drafting changes are needed to the sounding definition (beyond the pending reconfirmation that *"negotiating"* is not sounding); (vii) proportionate NCA application is important where there is compliance with local laws or there is otherwise limited substantive EEA nexus; (viii) the *"prior to the announcement of a transaction"* reference in the definition does not exclude bond issuance transactions that ultimately are not publicly announced; (ix) mandating audio recording only would further disincentivise sounding; and (x) removing the requirement for explicit market sounding recipient agreement to a disclosing market participant's written minutes would mitigate the cost and burden of sounding.

Regarding insider lists, the response noted: (i) the logistical burden of insider lists is a significant reason why many borrowers do not seek EEA trading admission; (ii) a single official identity number is sufficient to confirm the identity of a named individual in respect of the key purpose of insider lists (to evidence who was in possession of or had access to inside information at a specific moment in time); (iii) there might be scope for the *ex-ante* requirement for a person's contact details to be more limited (with such details provided on demand to regulators).

Lastly, regarding closed periods, the response noted that a blanket ban on new issuance arising from the extension of closed periods, from persons discharging managerial responsibilities (PDMRs), to issuers would be disproportionate.

ICMA will continue to engage on the review of MAR as it develops.

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The ESAs' consultation on the PRIIPs KID

CMU

On 16 October 2019, the European Supervisory Authorities (ESAs) published a joint consultation paper concerning amendments to the PRIIPs KID. Then on 24 October 2019, the European Supervisory Authorities (ESAs) issued a joint supervisory statement on the application of scope of the PRIIPs Regulation to bonds.

ICMA is working to respond to the consultation by the 13 January deadline. It is likely the response will not comment on amendments to the KID content requirements (since these have been previously confirmed as not having been developed with vanilla bonds in mind) but will flag that the product scope of the PRIIPs regime continues to be problematic.

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The IOSCO consultation on conflicts in debt capital raising

On 16 November 2019, IOSCO published a consultation report on conflicts of interest and associated conduct risks during the debt capital raising process. ICMA is working to respond to the consultation by the 16 February deadline. It is likely the response will *inter alia* re-iterate much of the published material previously flagged to IOSCO by ICMA in March 2018 (in the context of IOSCO's prior consultation on equity capital raising).

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ICMA Primary Market Handbook changes

Prospectus Regulation: With the help of leading law firms, ICMA has prepared draft updated versions of the following ICMA Primary Market Handbook items to reflect the new Prospectus Regulation:

- Appendix A8 Final terms and pricing supplement;
- Appendix A13 Selling restrictions and legends (EEA PRIIPs Regulation, EEA Prospectus Directive, UK); and
- Appendix A16 Sub-€100 denomination bonds under the EEA Prospectus Directive and retail cascade legends.

These materials have also been revised to take account of the UK's withdrawal from the European Union. The draft revised language is available from ICMA staff (legalhelpdesk@icmagroup.org) to ICMA members and ICMA Primary Market Handbook subscribers on request.

Deal announcements: On 17 December 2019, ICMA published new Appendix A5a on deal announcements in the ICMA Primary Market Handbook. This follows discussions between ICMA's syndicate and AMIC investor constituencies.

The purpose of new Appendix A5a is to facilitate, from January 2020, harmonisation of deal announcement presentation and minimum content. This, in turn, should help investors react more swiftly to such announcements (including through the use of machine-reading technology) in submitting their orders for new bond issues. Some market platforms maintain templates that investors may already consider to be substantively consistent in terms of this purpose.

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Asset-Backed Commercial Paper (ABCP)

Related to the EU STS Regulation, which has applied since 1 January 2019, on 16 October the European Commission published the RTS which it has adopted on transparency requirements for originators, sponsors and SSPE. This version of the RTS looks quite different to the revised draft published in January by ESMA, but we understand that the changes appear to be cosmetic rather than substantive. This adopted version of the RTS is subject to approval by the European Parliament and Council, following which the agreed final version will be published in the EU's *Official Journal* (OJ).

It is not expected that this approval process will lead to any significant changes, but as an initial review period of three months is applicable the actual OJ publication will most likely not happen until sometime in late February. This RTS will enter into force on the 20th day following that of its publication in the OJ, but as there is no provision for transitional relief market participants should already be making sure that they are prepared for the requirements which will then become applicable.

While there are some provisions of common application, there are three annexes which are specifically for ABCP (rather than non-ABCP) securitisations. These are Annex XI, Underlying Exposures Information - Asset-Backed Commercial Paper; Annex XIII, Investor Report Information – Asset-Backed Commercial Paper Securitisation; and Annex XV, Inside Information or Significant Event Information – Asset-Backed Commercial Paper Securitisation. Subsequently, on 20 December, ESMA published updated reporting instructions and XML schema for the templates set out in the technical standards on disclosure requirements.

On 6 November, Commission Delegated Regulation (EU) 2019/1851, of 28 May 2019, supplementing the EU STS Regulation with regard to RTS on the homogeneity of the underlying exposures in securitisation, was published in the EU's *Official Journal*. This Delegated Regulation, which – considering both ABCP and non-ABCP securitisations – sets out asset categories as well as a list of homogeneity factors available for the majority of the asset categories, subsequently entered into force, on 26 November.

In order to provide a comprehensive package of clarifications for market participants ESMA has developed a set of Q&A on the Securitisation Regulation, most recently updated on 15 November. The majority of Q&As in this document provide clarification on different aspects of the templates contained in the draft technical standards on disclosure which were recently published by the European Commission. In particular, the Q&As clarifies how several specific fields in the templates should be completed and also contains clarifications relating to STS notifications and securitisation repositories. It is important to be aware that ESMA has provided these Q&As in advance of some delegated acts being adopted by the Commission and may consequently be subject to change.

ESMA's website also provides a, gradually growing, list of the STS notifications it has received. Thus far the public transactions have all been non-ABCP transactions. However, of the 33 private transactions on ESMA's list, 25 are reported as being ABCP transactions, with 18 of these being in respect of trade receivables and the others being in respect of auto loans/leases (six) and leases (one).

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Market participants should already be making sure that they are prepared for the requirements which will then become applicable.

ICMA Primary Market Forum *by Katie Kelly*

Now in its 13th year, the annual ICMA Primary Market Forum (PMF) brings together a range of market participants active in the primary markets to discuss developments and trends. There was standing room only at this year's event, which was kindly hosted by the London Stock Exchange Group on 14 November.

The event started with a keynote speech on FinTech from Siegfried Ruhl, Head of Funding and Investor Relations, European Stability Mechanism (ESM). Starting with the premise that technological change should be viewed as an opportunity, rather than a risk, he considered that the primary markets lack a front-to-back straight-through-processing solution. He suggested that harnessing and engaging with new technology allows us to retain more control over it, whereas a more passive approach denies us the opportunity to mould it to the market's advantage. The ESM has successfully achieved this by identifying where FinTech can be efficiently applied for them; this includes in investor relations, bond allocations and assessing how bonds are traded.

This keynote speech was followed by a "fire-side chat" between Farnam Bigdoli, Head of Sustainable Finance at HSBC, and Jean-Marc Turchini, Head of Corporate Finance, Engie. Together, they shared insights into the sustainable finance universe, including the importance of having a strong sustainability issuance profile which aligns with global goals. Much of this is driven by the buy side, which is a strong impetus for issuers to be as sustainable as possible in order to remain investible. There are of course also significant political and regulatory drivers, which require careful management of the direct impacts of regulation and heightened disclosure regimes. Jean-Marc Turchini highlighted some of the practicalities of issuance, such as documentation issues, verification, compliance and reporting systems. Overall reputation management is of course critical – from devising a sustainable strategy and building a solid ESG reputation, to ensuring alignment with fast-moving market developments and evolving regulation.

A panel session followed, in which an issuer (Peter Green, Lloyds), an investor (Ketish Pothalingam, PIMCO), a lawyer (Amanda Thomas, Allen & Overy), a syndicate manager (Jean-Marc Mercier, HSBC) and a fixed income specialist (Darko Hajdukovic, London Stock Exchange) participated in a lively debate on a variety of issues, such as the effects of risk categorisation under the Prospectus Regulation, and whether the new regime affects the liability dynamic as between the issuer, the investors and the listing authority. The panel also discussed whether the market is doing enough to deal with the transition to risk-free rates, and by reference to recent activities in transitioning LIBOR floating rate notes to SONIA by way of consent solicitation, considered some of the remaining challenges in addressing the stock of LIBOR-linked bonds outstanding beyond 2021. Sustainability also featured, with the panel deliberating whether the overlay of policy and regulatory interventions was potentially confusing to the market, and if it would inadvertently stifle potential growth. This is hard to assess, and all agreed that while growth in the sustainable financing is extremely healthy, it has by no means reached a pinnacle either in terms of innovation (such as blue bonds, SDG-linked bonds and transition bonds) or regulation.

The event wrapped up with a discussion on diversity, inclusion and well-being with Mark McLane, Head of Diversity, M&G plc. He considered that diversity, inclusion and well-being are as important as any other business metric and recommended that firms capture and use data in a meaningful way to measure the success of their diversity programmes and initiatives. Mental health and well-being now feature on the agenda of many firms, and he helpfully highlighted the various toolkits available to equip firms to deal sensitively with the associated issues.

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Secondary Markets



by Andy Hill, Elizabeth Callaghan and Gabriel Callsen

CMU A consolidated tape for EU bond markets

Introduction

The concept of a consolidated tape originates from equity markets in the US and dates back to the late 1970s. The purpose of the consolidated tape was to provide an aggregate view of trade and quote information of equities in real time across stock exchanges.[1] In US fixed income markets, a consolidated tape was set up in 2002 in the form of the Trade Reporting and Compliance Engine (TRACE) which is operated by FINRA, disseminating transaction data for a diverse range of debt instruments in real time.

In Europe, the Capital Markets Union (CMU) recognised the importance of a consolidated tape for financial markets under MiFID II, which "should increase the attractiveness of the EU capital markets as investment destinations."[2] In its report of October 2019,[3] the CMU High-Level Group recommended the establishment of a single Consolidated Tape facility:

"Achieving a Consolidated Tape would make all European market data easily accessible both for professional and retail investors and increase trust for cross-border investments. The European Commission should specify criteria for a single Consolidated Tape covering all execution venues in a delegated act based on MiFID II. Enhancing the quality of market data is needed to make such a tape useful. Such a facility should be non-profit, fall under the responsibility of ESMA."

Greater transparency in OTC bond markets and other non-equity asset classes is also stated as one of the key objectives of MiFID II and MiFIR.

Drivers for a consolidated tape - bond/equity markets: While bond markets and equity markets share a few challenges – such as fragmentation of infrastructure, and an unlevel playing field that benefits those who can afford to pay for data – it is widely understood that their ecosystems are profoundly different. One only has to view the asset classes' market structure and protocols to see the differences: Request-for-Quote (RFQ) protocols in fixed income versus order books for equities; OTC trading (more OTC trading than on-venue trading in bonds) versus local equity exchanges; and the fact that there are approximately thirty-three times more listed bonds than listed equities in Europe.

These differences suggest that the drivers for a consolidated tape (CT) in these markets are also different. For bonds, the rationale is principally the need for a true consolidated overview of the market that is reliable, accessible and trustworthy, while in equities, cost and speed are the issues, assisting with arbitrage prevention and market data costs.

What are the benefits of an EU bond consolidated tape? The goal of the bond CT is to improve transparency, assist decision-making and provide market insights to end-investors, large or small. Adoption of the appropriate structure would benefit the whole market, by providing

1. https://www.nyse.com/data/cta; https://www.ctaplan.com/index

2. *An Action Plan on Building a Capital Market Union* (2015), European Commission

3. See: https://nextcmu.eu/wp-content/uploads/2019/10/The-Next-CMU-HL_DO.pdf

a centralised, high quality, affordable, trustworthy data source, offering a comprehensive market view. This would bring immediate benefits to the professional bond market but could also benefit the retail sector more widely as the service develops.

Potential benefits of a consolidated tape:

- *Facilitating more accurate assessments of execution quality:* A post-trade CT can be used for transaction cost analysis and best execution assessments, as it provides a neutral and reliable source of current market trading activity against which to reference execution quality. Evidencing best execution is also generally a compliance requirement, where again the existence of a CT could support observance.
- *Levelling the playing field with respect to access to information:* A post-trade CT removes existing information asymmetries, where certain market participants may have greater visibility regarding ongoing trading activity than other investors. This enables investors to assess more accurately current market dynamics, increasing overall investor confidence, particularly during times of market volatility.
- *Promoting competition:* By enabling investors to compare the prices they receive from liquidity providers with concurrent trading activity across the market, a post-trade CT promotes price competition as investors are able to demand more accountability from their liquidity providers. In addition, new liquidity providers are more likely to enter the market, as they are able to access information regarding current market dynamics, including trading volumes and pricing, on an equal basis as existing liquidity providers.
- *Promoting market resiliency: The* removal of existing information asymmetries contributes to market resiliency by ensuring that changes in supply and demand are more efficiently reflected in current price levels. In addition, without a neutral and reliable source of current market trading activity, investors may be more likely to pull back during times of volatility.
- *More accurate pricing of derivatives:* Prices in derivatives, such as futures, options, and credit default swaps, should reflect the value of the *underlying cash instruments*. Where it is difficult to find accurate market valuations of the underlying security, derivatives pricing can diverge from fair value, creating additional risks and costs for investors looking to hedge their exposures. Improved transparency in bond markets will therefore help to facilitate more accurate pricing, and potentially greater liquidity, in related derivatives.
- *Improved fund valuations:* The accuracy and immediacy of fund valuations is directly contingent on the ability to value accurately the underlying securities. Improved transparency in bond markets will help managers to maintain accurate valuations of their fixed income funds. This equally applies to fixed income exchange traded funds (ETFs) and would help to maintain a closer relationship between the net asset value (NAV) of the underlying fund and the price of the related ETF through better facilitation of the creation and redemption process.
- *Facilitating automation:* Greater efficiencies in bond markets can be achieved through the automation of many processes, including the pricing and execution of orders. The ability to automate such processes successfully is contingent on comprehensive, accurate, and timely market data, which a CT would go far in providing.
- *Supporting the CMU:* A post-trade CT for bonds strengthens EU capital markets by linking together the disparate trading venues and APAs across the EU, enhancing investor confidence due to increased transparency in the market. Stronger and more liquid EU capital markets promote capital formation, job creation, and economic growth.

Why has an EU bond consolidated tape not emerged? Efforts to develop a consolidated tape have been unsuccessful in the past due to concerns around the high costs for its development in a restrictive regulatory environment with a lack of clear commercial benefits for the consolidated tape provider (CTP), despite widespread demand from market participants. MiFID II laid out requirements for the "voluntary" establishment of CTPs, thereby paving the way for multiple rather than a single CTP. Furthermore, the fact that MiFID II does not mandate the submission of transaction data to CTPs, as is the case in the US, is considered to be a key hindrance for the emergence of a consolidated tape. In other words, there is no commercial incentive for potential CTPs to acquire the post-trade data, nor for APAs to provide the post-trade data to a CTP.

Current state/end state

In order to obtain a clear view of an EU bond consolidated tape, it is necessary to compare and contrast the current state of aggregation and consolidation of post-trade data in the EU with the desired end state for EU post-trade data consolidation. This includes observations of TRACE bond consolidated tape in the US.

(i) Current state

How usable is the post-trade data? Post-trade data is currently scattered across more than seven (bond) APAs, which makes aggregating the data extremely challenging due to difficulties accessing the "public" websites, a lack of consistency in formatting, and data errors.

Due to high level of data cleansing, costly and inefficient process of acquiring the data, post-trade data is not useable yet, according to the buy side. In time, buy sides see potential for transaction cost analysis when data quality improves. Additionally, the sell side believes that because of delays, exacerbated by the extra aggregation and cleansing layers (cleansing, format differences, data errors, extreme values, data spikes etc), price discovery benefits are currently limited. However, today there is some degree of price discovery.

What is the view from across the pond? While participants observe both pros and cons of the US bond consolidated tape, TRACE, the overall impacts are largely perceived to have been positive for market efficiency and liquidity. In particular, the gradual and phased-in approach, with the ability to review and adjust adaptation, is viewed as being an identifiable advantage of the implementation process.

Below are specific examples of what EU bond markets should borrow from US TRACE:

- Communication and consultation with stakeholders to validate changes on a technical level.
- Gradual roll-out of CT by (sub)asset class.
- Uniformity of reporting requirements and publication of technical specifications.
- Analysis of data to maintain robust data quality standards, *prior* to public dissemination of data.
- Testing and phase-in procedures for introduction of changes (such as new reporting fields).

(ii) Desired end state

- The post-trade CT should aim to provide a comprehensive, detailed, accurate and meaningful view of where, when and how all trades occurred. Furthermore, the scope of the bond CT should cover 100% of all bond instrument transactions and volumes across all trading venues and APAs.
- *Scope and level of information per/instrument to be reported:* Raw post trade data - date, time of execution, reported date & time [taking into account current publication and deferral obligations under MiFID II], ISIN, price, venue, cancel or correction. While the CT should have execution prices (taking into account MiFID II's deferrals) as a mandatory data item in the CT, additional data items such as yields will in all likelihood be required by market participants. Therefore, once there is a consolidated view of prices in the CT, the CT provider (CTP) could then derive yields which are fundamental data points in the relative valuation of bonds and comparative analysis of best execution.
- *Mandatory submission:* It is essential that the responsibility for data feed provision should be changed from the CTP's obligation to obtain data to stating that all trading and execution venues and APAs have an obligation to provide data to the CTP (incentives possibly considered). This would require amendments to the Level 1 text of MiFID II.
- The timing of dissemination should be in line with the existing MiFID II post-trade transparency regime. However, harmonisation of MiFID II deferral regimes (including the optimisation of aggregation and omission rules) across the EU should be considered in order to avoid fragmentation and ensure a level playing field for all EU market participants.
- The day-to-day operation of a consolidated tape should be conducted by an entity other than ESMA or the Commission. Under this approach, the CTP contract should be awarded to a third-party provider with a high level of data management experience as well as related knowledge of the asset class (bonds). The contract should be awarded for no less than five years, the firm awarded the contract should have robust conflict-of-

The removal of existing information asymmetries contributes to market resiliency by ensuring that changes in supply and demand are more efficiently reflected in current price levels.

interest rules, and costs to industry participants should be kept to a minimum.

- ESMA or the Commission should have oversight of the CTP contract and monitor for any breach of contract: eg data quality, access, pricing etc. Industry participants (buy-side, sell-side and retail) should advise with market functioning expertise.
- The CTP should own the raw data and make it available to all market participants through a minimum-cost utility model. The CTP should not be prevented for charging market participants for optional enriched data services. There should be robust conflict of interest rules for the CTP and any CTP additional data service offerings, outside the low-cost utility raw data CT offering to market participants.
- Alternatively, ESMA could consider creating a single consolidated bond tape which they govern and operate as a minimum cost "utility" for users.

Setting the stage for an EU bond consolidated tape: next steps

In early December 2019, ESMA recommended a real-time consolidated tape for equity markets. ESMA published *first review* on the development of prices for market data and on the consolidated tape for equity, following the application of MiFID II for nearly two years.

For ESMA, the main reasons why a market-led equity consolidated tape failed to develop are the limited commercial rewards to potential providers within the current regulatory framework, as well as possible competition by non-regulated entities such as data vendors.

In order to establish a real-time consolidated tape [for equity markets], the following *key factors* are necessary:

- a high level of data quality;
- the mandatory contribution of data by trading venues and APAs to the consolidated tape;
- the consolidated tape sharing revenues with contributing entities; and
- a strong governance framework.

The establishment of an EU-wide real-time consolidated tape is a technically demanding task which will require a substantial investment of both time and resources by all parties involved, including the need to change the legal framework.[4]

This ESMA announcement may be in relation to an equity consolidated tape, however the same reasoning as to why a bond consolidated tape has not yet emerged and the key factors necessary for an equity consolidated tape apply also to EU bond markets.

Moreover, and of note, ICMA is currently in dialogue with the European Commission regarding the potential establishment of a bond consolidated tape in the EU.

Taking everything into account, it appears the way is open for the creation of a single consolidated tape for EU bond markets.

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MiFID II/R: ESMA guidance in the fourth quarter of 2019

In the fourth quarter of 2019, the European Securities and Markets Authority (ESMA) issued further guidance in relation to MiFID II/R. The following briefing is designed to provide a non-exhaustive summary of selected guidance impacting market structure and fixed income trading, notably: (i) liquidity assessments of bonds for Q3 2019 for transparency purposes, (ii) publication of data for the SI calculations for bonds, (iii) best execution: publication formats and accessibility of RTS 27 and RTS 28 reports, (iv) further ESMA guidance including investor protection, transparency and MiFIR data reporting topics, (v) MiFID II/R and Brexit: ESMA update on preparations for a possible no-deal Brexit, and (vi) 2020 calendar of relevant publications for the transparency regime and SI calculations.

MiFID II/R: Q4 2019

Overview of selected ESMA guidance:

6 December: Q&As on MiFIR data reporting

5 December: Q&As on transparency topics

4 December: Q&As on investor protection and intermediaries topics

8 November: Liquidity assessments for individual bonds by ISIN for Q3 2019

8 November: Completeness indicators related to bond liquidity data

8 November: SI calculations for bonds

7 October: ESMA update on preparations for a possible no-deal Brexit

3 October: Q&As on investor protection and intermediaries topics

2 October: Q&As on transparency topics

4. ESMA, 5 December 2019.

(i) Liquidity assessments of bonds for Q3 2019 for transparency purposes

On 8 November 2019, following an announcement on 30 October, ESMA made available the quarterly liquidity assessment for bonds under MiFID II/R through FITRS in XML format and the FITRS interface. Accordingly, 611 bonds were deemed liquid in Q3 2019. The liquidity assessments are applicable from 16 November 2019 until 15 February 2020. However, ESMA stated that "additional data and corrections submitted to ESMA may result in further updates within each quarter, published in ESMA's FITRS, which shall be applicable the day following publication."

(ii) Publication of data for the SI calculations for bonds

On 8 November 2019, ESMA released the data for the systematic internaliser (SI) calculations for bonds, equity and equity-like instruments: "More specifically, ESMA has published the total number of trades and total volume over the period April-September 2019 for the purpose of the systematic internaliser (SI) calculations". The list of ISINs released by ESMA comprises 334,610 bonds and 22,015 equity and equity-like instruments. "The results are published only for instruments for which trading venues submitted data for at least 95% of all trading days over the 6-month observation period. The data publications also incorporate OTC trading to the extent it has been reported to ESMA." Investment firms were required to perform an internal assessment against the data provided by ESMA, and if in scope of the SI regime, comply with relevant SI obligations from 15 November 2019. Further information on the SI regime and calculations are available on ESMA's website.

(iii) Best execution: publication formats and accessibility of RTS 27 and RTS 28 reports

On 3 October 2019, ESMA provided further clarifications on how RTS 27 and RTS 28 reports should be made public [Section 1, question 8]. Accordingly, "in order to ensure that such reports are in the public domain and freely accessible, firms can publish these reports on their respective websites in an easily identifiable location on a page without any access limitations. ESMA notes that these reports should not be placed behind a firewall, registration page or be subject to password encryption or other restrictions. Venues and firms should also ensure the readability and comprehensibility of these reports to provide the public with relevant data on execution quality. Therefore, venues and firms should provide the RTS 27 and 28 reports in an electronic format that allows for computerised calculations and mass processing that is compatible with standard and easily accessible machine-reading processes, to fulfil the requirements of (i) being "machine-readable" and (ii) enabling the public to search, sort and analyse all the provided data".

(iv) Further ESMA guidance and Q&A updates

With regard to investor protection topics, ESMA provided further guidance on 3 October 2019 on how the term "ongoing relationship" should be interpreted [Section 15, question 1]. Other Q&As issued on 4 December 2019 relate to the application of *ex-post* costs and charges disclosure requirements to portfolio management [Section 9, question 31] and product intervention [Section 17, question 1]. Transparency-related questions on the conversion of LIS/SSTI thresholds in lots for derivatives such as futures/forwards and options have been addressed in Q&A updates on 5 December [Section 4, question 19].

[Best ex] reports should not be placed behind a firewall, registration page or be subject to password encryption or other restrictions."

Furthermore, ESMA published on 8 November 2019 the quarterly completeness indicators related to bond liquidity data submitted by trading venues. In a Q&A update on MiFIR data reporting published on 6 December 2019, ESMA clarified the requirements for submission of the new reference rate €STR which is not included in RTS 22 [Transaction reporting] and RTS 23 [Reference data], under Article 26 and Article 27 of MiFIR.

(v) MiFID II/R and Brexit: ESMA update on preparations for a possible no-deal Brexit

On 7 October 2019, ESMA published an update on the UK's withdrawal from the European Union - preparations for a possible no-deal Brexit scenario on 31 October 2019: *Public Statement on the Use of UK Data* in ESMA databases and performance of MiFID II calculations, *Public Statement on the Impact of No-deal Brexit* on MiFID II/MiFIR and the Benchmarks Regulation (BMR) – C(6) carve-out, ESMA opinions on third-country trading venues for the purpose of post-trade transparency and position limits, post-trade transparency for OTC transactions, BMR ESMA register of administrators and 3rd country benchmarks calculations, as well as a *Public Statement on Operational Plans* related to ESMA databases and IT systems.

(vi) 2020 calendar of relevant publications for the transparency regime and SI calculations

On 19 December 2019, ESMA furthermore published its 2020 calendar of MiFID II/MiFIR relevant publications for the transparency regime and systematic internalisers' tests. Key dates for bonds include the quarterly liquidity assessments and systematic internaliser calculations on 1 February, 1 May, 1 August and 1 November 2020. The annual transparency calculations are due to be published on 30 April 2020.

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CSDR mandatory buy-ins: ICMA's implementation work

CMU

On 14 November 2019, ICMA confirmed that it will amend its Buy-in Rules to support the implementation of the EU Central Securities Depositories Regulation (CSDR) mandatory buy-in provisions. ICMA Buy-in Rules are part of its Secondary Market Rules & Recommendations which are widely relied upon by ICMA members in the international bond markets. The ICMA Rules apply automatically to trades in international securities between ICMA members and are extensively used by firms operating in the international bond markets (both members and non-members) who generally apply the Rules by reference in their Terms of Business.

The CSDR buy-in provisions, which are due to come into force in September 2020 (although this may be delayed for technical reasons), create a mandatory obligation for trading parties to execute buy-ins against counterparties who fail to settle their trades within a required period. The regulatory technical standards also lay out a prescriptive process and timeline for the buy-in. The requirements will apply to trades that are intended to settle on EU ICSDs and CSDs. This will apply to all trading level entities settling trades on EU (I)CSDs, regardless of their location or jurisdiction. ICMA has published an information brochure which details the various regulatory requirements and obligations, as well as the scope of application.

While the CSDR introduces new regulatory requirements and features, the ICMA Buy-in Rules will be updated to support implementation of the CSDR buy-in requirements in the international bond markets, as well as providing market best practice for the buy-in process.

ICMA is also exploring a number of potential contractual provisions to enhance the CSDR buy-in framework and help mitigate some of the inefficiencies and market risks created by the Regulation. It is intended that utilising the ICMA Rules will address the asymmetric treatment to the settlement of the executed buy-in or cash compensation differential that has been identified as one of CSDR's thornier (and largely unintended) anomalies. ICMA is also holding the pen on a cross-industry initiative to design a pass-on mechanism, largely based on the existing ICMA pass-on framework, that can be incorporated into the revised ICMA Rules. The Regulation itself does not provide for pass-ons, which would result in every single fail, including linked transactions, triggering a unique (and unnecessary) buy-in.

ICMA intends to consult with its members and the broader industry on the proposed revisions to the ICMA Buy-in Rules in early 2020. The updated Rules will be introduced in parallel with the eventual application of the CSDR buy-in requirements.

Firms interested in ICMA's ongoing work and contractual solutions to support CSDR buy-in implementation and provide market best practice are encouraged to sign-up to the mailing list of ICMA's dedicated CSDR Settlement Discipline Working Group.

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The ICMA Buy-in Rules will be updated to support implementation of the CSDR buy-in requirements in the international bond markets, as well as providing market best practice for the buy-in process.

Updated ETP mapping directory

ICMA has updated its mapping directory of Electronic Trading Platforms (ETPs). The directory now lists a total of 43 electronic execution venues, Order Management Systems (OMS) and information networks. It is intended to help market participants understand what execution and non-execution venues are available for cash bonds. Included within the directory are brief descriptions of the system/platform, products in scope, price discovery mechanisms, trading protocols, geographical coverage, regulatory status and other additional services such as regulatory reporting under MiFID II/R.

The market has seen small movements with four additional platforms recently listed in the directory and four deletions. Two non-execution platforms are no longer supported and two MTF execution platforms were decommissioned in 2019. This may indicate a relative saturation of competition in an increasingly difficult market for new entrant platform providers. There is evidence of increased use of the transparency data produced by MiFID II/R requirements for analytics and new execution models. This follows the trend for platforms to increasingly leverage and enrich market data with the objective of providing the user with further insights to gain competitive advantages. The revised ETP mapping directory is available on ICMA's website.

The mapping directory does not constitute an exhaustive list of providers in the market. Relevant providers that are not yet covered by the mapping directory and wish to join are very welcome to do so.

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Recent secondary market research

OECD, 2019, Corporate Bond Markets in a Time of Unconventional Monetary Policy

Building on a dataset of almost 85,000 unique corporate bond issues by non-financial companies from 114 countries between 2000 and 2018, this brief report provides an overview of global trends in corporate bond issuance since the 2008 financial crisis. The paper documents a number of elevated risks and vulnerabilities associated with this development and looks at how the quality of today's outstanding stock of corporate bonds differs from earlier credit cycles. Bond ratings, bondholder rights and repayment requirements are areas of particular focus. The content and methodologies used will provide a basis for discussions within the OECD Corporate Governance Committee and with other experts about further work on corporate bonds as an important source of market-based corporate finance.

IMF, 2019, German Bond Yields and Debt Supply: Is There a "Bund Premium"?

The paper estimates the "Bund premium" as the difference in convenience yields between other sovereign safe assets and German government bonds adjusted for sovereign credit risk, liquidity and swap market frictions. A higher premium suggests less substitutability of sovereign bonds. The researchers document a rise in the "Bund premium" in the post-crisis period. They show that there is a negative relationship of the premium with the relative supply of German sovereign bonds, which is more pronounced for higher maturities and when risk aversion proxied by bond market volatility is high. Going forward, the expectation is for German Government debt supply to remain scarce, with important implications for the ECB's monetary policy strategy.

Converse, N., and Mallucci, E., 2019, Differential Treatment in the Bond Market: Sovereign Risk and Mutual Fund Portfolios (Board of Governors of the Federal Reserve System)

The researchers attempt to answer the question of how sovereign risk affects investors' behaviour using a novel database that combines sovereign default probabilities for 27 developed and emerging markets with monthly data on the portfolios of individual bond mutual funds. They first show that changes in yields do not fully compensate investors for additional sovereign risk, so that bond funds reduce their exposure to a country's assets when its sovereign default risk increases. However, the magnitude of the response varies widely across countries. Fund managers aggressively reduce their exposure to high-debt countries and high-risk countries. By contrast, they are more lenient toward core developed markets. In this sense, these economies appear to receive preferential treatment. Second, they document what determines the destination of reallocation flows. When fund managers reduce their exposure to a country in response to its sovereign risk, they shift their assets to countries outside the immediate geographic region while at the same time avoiding countries with high debt-to-GDP ratios and markets to which they are already heavily exposed. These results are supportive of models of sovereign default that assign a non-trivial role to the preferences of international creditors.

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ICMA Secondary Market Forum

The ICMA Secondary Market Forum brings together leading experts from the European fixed income market, representing banks and broker-dealers, investors and asset managers, as well as trading venues and technology providers. The Forum is an opportunity to hear, and participate in, discussions on the critical issues facing the European bond markets and the key drivers of evolving market structure and dynamics. Topics cover market liquidity, developments in e-trading, new protocols, and automation, the changing sell-side buy-side relationship, regulatory impacts (including MiFIR transparency and CSDR buy-ins), the growth of the fixed income ETF market, and the implications of monetary policy and renewed quantitative easing.

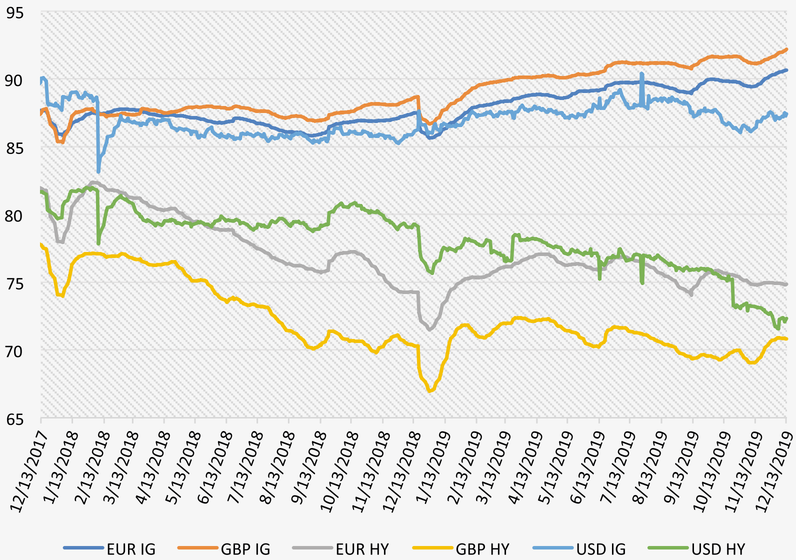
Building on the success of ICMA's inaugural Secondary Market Forum in Paris in 2019, the next Forum will take place in Amsterdam on the afternoon of 4 March 2020, kindly hosted by InsingerGilissen Bankiers. More details of speakers and panels will be made available on the ICMA events webpage in due course, along with registration details. There is no cost to attend and the Forum is open to both members and non-members. As well as an opportunity to engage with the key forces and trends driving and shaping Europe's secondary bond markets, the Forum is an excellent platform through which to interact and network with a broad range of market participants and experts from across Europe.

Places will be limited, but if you would like to register your attendance early, please contact Leigh Anne Cooke in the ICMA events team.

ICE Data Services Corporate Bond Market Liquidity Indicators™

December 2019

ICE Liquidity Indicators™



Source: ICE Data Services

Commentary

As discussed in previous Quarterly Reports, corporate bond market liquidity appears to show a sharp decline in Q1 2018, which largely correlates with the US led sell-off in global credit markets. But IG liquidity remained relatively rangebound throughout 2018 followed by a drop at year-end. Subsequently, liquidity levels rebounded swiftly in Q1 2019, and continued to improve steadily towards the end of Q4 2019 with the exception of US IG.

EUR and GBP, but also USD HY liquidity, however, showed a fairly steep decline throughout 2018 followed by a marked drop at year-end. Liquidity levels recovered throughout Q1 2019 but then followed a downward trend in Q3 2019 before improving again towards year-end. US HY liquidity was an exception with a marked decline from Q2 2019, reaching a new low in Q4 2019.

While it is difficult to attribute causality, a possible explanation for the deterioration in EUR HY liquidity in 2018 could be the announcement of the wind-down of the ECB's Corporate Sector Purchase Programme (CSPP). While HY is not in scope of the purchase programme, the sector has benefited from a "portfolio rebalancing" effect. Rate hikes in the US, widening CDS spreads and falling equities markets appear furthermore to have had a knock-on effect on reduced EUR and GBP liquidity.

At the beginning of 2019, a then stable outlook on monetary policy and tightening CDS spreads seem to have countered this effect. Meanwhile, the continued economic uncertainty arising from Brexit, global geopolitical tensions and a "flight-to-quality" appear to have had a continued adverse impact on HY liquidity throughout Q2 and Q3 2019. Liquidity in GBP HY, a segment dominated by UK retailers, appears to be particularly impacted by Brexit uncertainty in Q2 and Q3 but improved subsequently in the last quarter of 2019. A sell-off in global bond markets in Q4 2019 does not appear to have had a material impact on liquidity, but it remains to be seen to which extent the third rate cut by the Fed in 2019 and the ECB's relaunched asset purchase programme will impact corporate bond market liquidity going forward.

ICE Liquidity Indicators™
ICE Liquidity Indicators™ are designed to reflect average liquidity across global markets. The ICE Liquidity Indicators™ are bounded from 0 to 100, with 0 reflecting a weighted-average liquidity cost estimate of 10% and 100 reflecting a liquidity cost estimate of 0%. The ICE Liquidity Indicators™ are directly relatable to each other, and therefore, the higher the level of the ICE Liquidity Indicators™ the higher the projected liquidity of that portfolio of securities at that point in time, as compared with a lower level. Statistical methods are employed to measure liquidity dynamics at the security level (including estimating projected trade volume capacity, projected volatility, projected time to liquidate and projected liquidation costs) which are then aggregated at the portfolio level to form the ICE Liquidity Indicators™ by asset class and sector. ICE Data Services incorporates a combination of publicly available data sets from trade repositories as well as proprietary and non-public sources of market colour and transactional data across global markets, along with evaluated pricing information and reference data to support statistical calibrations.

Repo and Collateral Markets

by Andy Hill and Alexander Westphal

SFTR implementation

CMU Over the past months, market participants have eagerly awaited the publication of ESMA's important final Level 3 guidance on SFTR reporting, the last major missing piece to complete the regulatory framework. Following the consultation on the draft Guidelines over the summer, the final version of the document was initially expected in October, but this date then slipped. On 6 January, ESMA finally released the final guidance documents. Alongside the Reporting Guidelines, ESMA also published its Final Report and an updated version of the Validation Rules, defining whether a particular reporting field is optional, conditional or mandatory, as well as a statement on LEI codes. The latter grants reporting firms a 12-month grace period for the reporting of LEI codes for issuers from non-EU countries. This requirement had been raised by ICMA and other industry stakeholders as a particular concern, given the large gap in LEI availability at a global level. The suite of Level 3 guidance is completed by another important document which had been published by ESMA already before Christmas: the ISO20022 XML schemas for SFTR reporting. The schemas specify standardised message formats to be used for the communication between reporting firms and their TR, but also between TRs and between TRs and authorities. A focus over the next few weeks will be to review the different guidance documents in detail and to seek further clarity from ESMA where required.

In addition, ICMA also continues to push ahead with the detailed work with its members to prepare for the implementation. This work is supported by ICMA's dedicated SFTR Task Force, an open forum which has been created to drive the industry's implementation efforts for repos. The SFTR TF brings together representatives from a broad range of nearly 150 firms, including market participants and infrastructures but also all the key vendors and trade repositories. The key objective of ICMA and the SFTR TF is to develop detailed best practice recommendations for reporting under SFTR to complement the regulatory framework and provide additional guidance for members. The best practices are collated in ICMA's SFTR Guide. While currently still an internal draft, it is planned to publish the document more widely as soon as the final ESMA Guidelines have been incorporated into our own recommendations. A launch event for the Guide is currently planned in early 2020. Details will be announced shortly.

Besides SFTR itself, the SFTR Task Force has also been working on a separate but closely related issue, the reporting requirements under MiFIR for repos with EU central banks. While these transactions are exempt from SFTR reporting they have unfortunately been brought into scope for MiFIR reporting, which creates a number of practical challenges as the MiFIR framework was not designed with SFTs in mind. Over the past months, ICMA's SFTR Task Force has discussed the issue, considered various different options and put together a proposal for the reporting of these repos under MiFIR. On 29 November, the proposals, which were coordinated with other trade associations, were submitted to ESMA for validation.

Finally, important aspects of the SFTR implementation work continue to be awareness raising and education. Since July, ICMA has held a number of regional events and technical workshops on SFTR. Most recently, ICMA, in collaboration with ICMA's Luxembourg region, hosted the *ICMA Seminar - Getting Ready for SFTR* in Luxembourg. ICMA is also holding regular full-day workshops on SFTR reporting which are more technical in nature and aim to provide participants with an in-depth understanding of the practicalities of SFTR reporting, including the key SFTR requirements as well as ICMA's best practice recommendations. The next editions of the workshop are scheduled for 22 January in London and 18 February in Frankfurt For further information on ICMA's SFTR work, please check our SFTR webpage or get in touch by e-mail.

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CMU European Commission consultation on Basel III

At its meeting on 14 November, the ERCC Committee agreed that it should respond to the European Commission's consultation paper on *Implementing the Final Basel III Reforms in the EU*, with particularly attention to section 2, which relates specifically to securities financing transactions with questions focussing on: (i) minimum haircut floors for SFTs; (ii) other revisions to the calculation of the exposure at default for SFTs; and (iii) implementation challenges and administrative burden.

The ERCC response draws largely on the 2018 report, *GFMA and ICMA Repo Market Study: Post-Crisis Reforms and the Evolution of the Repo and Broader SFT Markets*, and the work undertaken by the associations with respect to the framework for minimum haircut floors.

Minimum haircut floors

The ERCC appreciates the objective of the FSB framework to limit the possible build-up of leverage outside the banking system and reduce the procyclicality of that leverage. The ERCC further recognises that the framework is intended to serve as a backstop in benign market conditions and is not intended to deter market participants from determining their own appropriate, more granular haircut schedules. However, there are a number of considerations in relation to which the framework appears to be overly punitive or unhelpfully complex, and which potentially undermine its effectiveness. In its response the ERCC highlights and discusses the disproportionate impact on risk weightings, netting anomalies, and the scope of application with respect to unregulated counterparties.

In particular, the ERCC is keen to stress that the framework provisions do not sufficiently differentiate between SFTs that are executed solely for the purpose of financing (which increase leverage) and those that are executed for other reasons, in particular borrowing and lending in specific securities. These transactions are essential in supporting market making activity, where liquidity providers are required to make short sales to service their clients, while also ensuring settlement efficiency. Facilitating short sales in cash securities is also essential for maintaining derivate market liquidity and price efficiency.

The ERCC urges the European Commission to review the potential unintended consequences of the minimum haircut floor framework, particularly with respect to market liquidity, efficiency, and stability, in light of the objectives of the CMU. As outlined in the 2017 report of the European Commission's Expert Group on Corporate Bond Markets, functioning, liquid repo and securities lending markets are a vital component in establishing an integrated, efficient, and resilient EU corporate bond market.

To that end, the ERCC also concurs with the EBA recommendation of taking a cautious approach before proceeding with the implementation in the EU of the minimum haircut floors framework, and agrees that further quantitative analysis of the potential impacts of the framework on lending and borrowing activity is required, as well as an assessment of the consequences for broader capital market functioning and efficiency.

Other revisions to the calculation of exposure at default for SFTs

The ERCC notes that the Basel III treatment of risk weightings for SFT exposures to banks under the standardised approach (SA) provides an adjustment for short-term exposures (under three months). The SA, however, does not provide for maturity sensitivity in the case of SFT exposures with non-banks. This overlooks the predominantly short-dated nature of the SFT markets and the inherent safety of short-dated collateralised transactions. This is likely to prove to be an unintended deterrent to banks transacting in SFTs with non-banks, potentially restricting access to key participants, such as pension funds, insurance funds, and corporates.

The full ERCC response on *Implementing the Final Basel III Reforms in the EU* was submitted ahead of the 3 January 2020 deadline.

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Other repo and collateral regulatory developments

Basel III and CVA

On 6 December 2019, the European Banking Authority (EBA) published two reports:

- *Basel III Reforms: Impact Study and Key Recommendations;*
- *Policy Advice on the Basel III Reforms on Credit Valuation Adjustment and Credit Risk.*

Of possible note and interest is the EBA recommendation that SFTs be removed completely from the CRR (Capital Requirements Regulation) CVA (credit valuation adjustment) framework, where they are fair-valued for accounting purposes. Currently, CRR provides an exemption whereby fair-valued SFTs are only brought into scope of the requirements where relevant national competent authorities deem the underlying CVA risk to be material. This deviates from the Basel III requirements which do not provide the possibility for such a discretionary exemption. The EBA recommends that a harmonised approach would be preferable, and that removing SFTs from scope altogether could be a better alternative to re-inclusion (as per Basel III), both at the EU and Basel levels.

This is outlined in section 1.6 (pages 52-59) of the policy advice report:

"157. Consistently with policy recommendation 2 put forward by the EBA in its report on CVA, the EBA supports the inclusion of fair-valued SFTs in the scope of the own funds requirements for CVA risk as set out in the Basel III post-crisis reforms standards published in December 2017, as this would harmonise the treatment of SFTs for the purposes of CVA risk. The EBA, however, also recognises that the efforts and operational challenges of implementing the revised CVA framework for SFTs may not be commensurate with the CVA risks stemming from SFTs to be captured for prudential purposes.

"158. At the same time, the EBA is concerned to introduce a discretion to exclude (or include) SFTs in scope of the CVA risk charge based on the materiality of the CVA risk stemming from the SFTs held by a particular institution, as this would involve operational challenges when assessing the materiality, and would undermine the level playing field in – and run against harmonising the treatment related to – the scope of transactions subject to the CVA risk charge. In this regard, removing SFTs altogether from the scope of the CVA risk framework (with no discretion to include them in its scope) would provide greater harmonisation than the introduction of the discretion to include or exclude SFTs in the scope of the CVA risk charge, and could thus represent a better alternative than the re-inclusion in the standards of such discretion, particularly considering the materiality of CVA risk stemming from SFTs and the operational challenges to calculate capital requirements against that risk. These aspects should be considered in the finalisation of the CVA risk framework at international level and in the specification of the treatment to ultimately be applied in the EU."

A quantitative impact analysis of the proposed changes to the CVA treatments can be found in section 4.2.1 (pages 34-37) of the impact study report.

It should also be noted that in the November 2019 *BIS Consultative Document on Credit Valuation Adjustment Risk: Targeted Final Provisions* the BIS proposes "to exclude from the scope of CVA capital requirements those SFTs where the CVA loss exposures are immaterial. This would relieve the operational burden of the framework."

Updated FSB framework for SFT haircuts

On 26 November 2019, the FSB published an updated version of its 2015 *Regulatory Framework for Haircuts on Non-centrally Cleared Securities Financing Transactions.*

Of note, the updated version incorporates the revised timelines for implementation of the numerical haircut floors for bank-to-non-bank (January 2022) and non-bank-to-non-bank (January 2024) transactions, as previously announced in July 2019.

BCBS Consolidated Basel Framework

On 16 December 2019, The Basel Committee on Banking Supervision launched its consolidated Basel Framework. The framework brings together all of the Basel Committee's global standards for the regulation and supervision of banks and presents them on a new section of its website. The full publication of the framework sets out the changes that the Committee agreed to make relative to the draft version of the framework and lists the new frequently asked questions and answers (FAQs) added to the framework since its publication in draft form in April 2019.

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Recent repo and collateral research

BIS Quarterly Report, December 2019

The December 2019 edition of the BIS Quarterly Report features two reports on the repo markets:

September Stress in Dollar Repo Markets: Passing or Structural?

The report points to changes in market structure and balance sheet composition as the main cause of the recent volatility in the US repo market, noting that at the end of Q2 2019 the largest four banks accounted for 50% of bank holdings of US Treasuries and only 25% of reserves. The article further argues that the September spike in repo rates may have been exacerbated by increased activity by non-bank participants: namely hedge funds entering basis positions, and money market funds providing short-term funding via sponsored clearing (who subsequently pulled their funding due to corporate tax drawdowns).

Euro Repo Market Functioning: Collateral is King

The report uses transaction-level data for centrally-cleared euro-denominated repos to analyse euro repo market performance since the mid-2000s. The researchers conclude that the Europe repo market proved resilient to both the 2008 financial crisis and the ensuing stress in the euro area sovereign market. However, their analysis shows signs of segmentation along the lines of the collateral used, with individual traders (banks) tending to specialise in one or just a few collateral segments, and liquidity and pricing efficiency tending to be more fragile in some segments than in others, depending on circumstances. It further observes that, in recent years, the euro repo market has been driven more by the needs of investors seeking particular securities as collateral rather than by investors seeking to trade liquidity. This trend has gained force from the ECB's purchases of government bonds as it seeks to provide additional monetary stimulus.

In addition, a Bank of England Staff Working Paper in December 2019 is relevant:

Simulating Liquidity Stress in the Derivatives Market

The study investigates whether margin calls on derivative counterparties could exceed their available liquid assets and, by preventing immediate payment of the calls, spread such liquidity shortfalls through the market. Using trade repository data on derivative portfolios, the researchers simulate variation margin calls in a stress scenario and compare these with the liquid-asset buffers of the institutions facing the calls. Where buffers are insufficient it is assumed that institutions borrow additional liquidity to cover the shortfalls, but only at the last moment when payment is due. Such delays can force recipients to borrow more than otherwise, and so liquidity shortfalls can grow in aggregate as they spread through the network. However, the research finds an aggregate liquidity shortfall equivalent to only a small fraction of average daily cash borrowing in international repo markets. Moreover, the study finds that only a small part of this aggregate shortfall could be avoided if payments were coordinated centrally.

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ICMA ERCC AGM

On 14 November, ICMA's European Repo and Collateral Council (ERCC) held its latest General Meeting. The event was kindly hosted by Euroclear in Brussels, directly following their Annual Collateral Conference. The format of the event differed slightly from previous years and consisted of two panel discussions. In a first panel, ICMA experts reviewed significant market developments in 2019 and the initiatives undertaken by the ERCC in support of the market. This included updates on the ERCC's implementation work in relation to SFTR and CSDR, the transition from EONIA to €STR, the latest legal developments as well as the ongoing work with ISDA to extend the Common Domain Model (CDM) to SFTs. A second panel focused on a more specific topic, discussing the prospects for "Creating a European Safe Asset". The panel was moderated by ICMA's Andy Hill, who was joined by senior representatives from both the official and the private sector. More details on the agenda as well as all the presentations are available on the ICMA website.

As part of the programme, ICMA's Richard Comotto presented the results of the latest, 37th edition of the semi-annual European Repo Market Survey, which was released on 13 November. The survey, which calculates the amount of repo business outstanding on 5 June 2019, from the returns of 55 offices of 51 financial groups, sets the baseline figure for the size of the European repo market at €7,761 billion, a decrease of 1.1% since the December 2018 survey, but an increase of 5.6% year-on-year.

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Master Regulatory Reporting Agreement *By Lisa Cleary*

ICMA has jointly published the Master Regulatory Reporting Agreement (MRRA), in association with AFME, FIA, ISDA and ISLA. An explanatory memorandum has been published alongside the agreement.

The MRRA provides users with a template agreement for documenting regulatory reporting arrangements in relation to derivatives and securities financing transactions entered into under standard industry documentation, such as the Global Master Repurchase Agreement (GMRA).

EMIR (as amended by EMIR REFIT) and SFTR impose delegated and mandatory reporting obligations on parties entering into derivative and SFT contracts, respectively. The MRRA has been structured on a modular basis (see below), featuring various schedules, a Derivatives Annex (in relation to EMIR) and a Securities Financing Transactions Annex (in relation to SFTR). Parties can assemble an agreement which is appropriate for their trading relationships and reflects their regulatory obligations.

The SFTR reporting obligations will be phased in over a nine-month period, from 14 April 2020. Ahead of the relevant go-live date, parties may wish to put an MRRA in place to document their reporting arrangements. Parties may delegate their reporting obligations and/or may also be involved in trading relationships which give rise to mandatory reporting requirements. Both arrangements are catered for in the MRRA, via tailored elections which the parties will need to agree. The agreement also provides an election for automatic transition from mandatory to delegated reporting.

ICMA has been at the forefront of efforts to understand the operational impact of the SFTR, providing practical guidance on reporting requirements. The publication of the MRRA adds to the body of knowhow made available to ICMA members. More information is available at the ICMA website.

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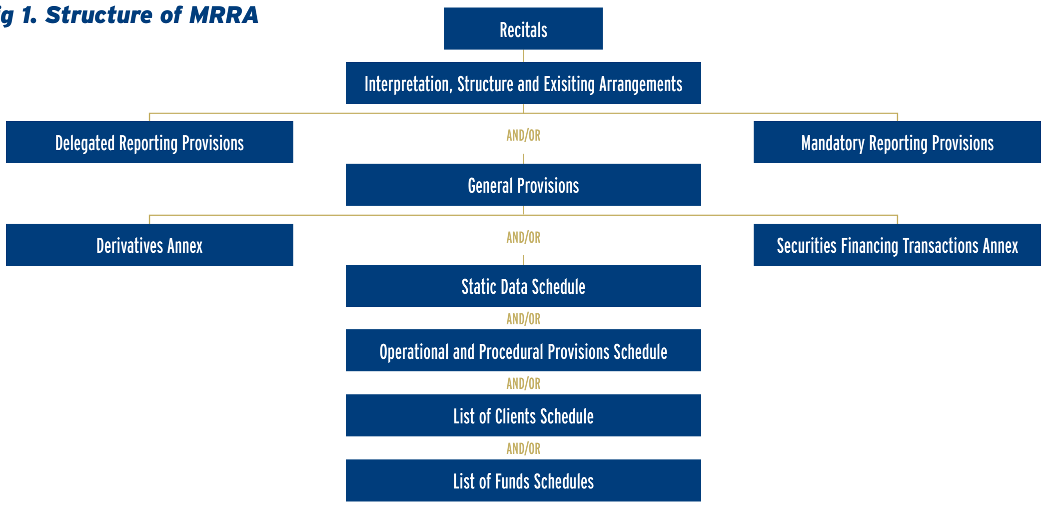
Fig 1. Structure of MRRA



Source: Explanatory Memorandum to the Master Regulatory Reporting Agreement available on ICMA website

The registration and depository system in China's bond market

By Echo Jiang, CCDC, and Ricco Zhang

China's domestic bond market is the second largest in the world and is accessible to foreign institutional investors. In the course of the development and opening-up of the bond market, however, some have had the impression that the depth of market access to be inadequate; in particular, that the registration and depository system is still not effectively aligned with the international market. To address this issue, this article analyzes the differences in the registration and depository systems between China and the international market and the underlying reasons from a legal perspective, including a discussion of concepts of "registration" and "depository" as well as their historical background as the logical starting point for this research. On this basis, the compatibility between China's bond market and international conventions is discussed, and a registration and depository arrangement that accommodates both the business practice of foreign investors and China's particular market environment is explored.

Historical background of the securities registration and depository system

The registration and depository system of a securities market is a set of institutional arrangements concerning the identification and exercising of securities rights, as well as related services arrangements. The concept of "depository" arose in the era of paper-form securities when owners of securities wished to outsource the custody of their securities to a third party. Banks and other institutions acting as the third-party custodian then became the nominal owners of the securities and took instructions from the beneficial owners. Meanwhile, the demand arising from market players for the immobilization of securities, to improve the efficiency of post-trade processing, led to the establishment of central securities depositories. The advancement of computer technology made the delivery of physical instruments a thing of the past, and eliminated any possibility of securities forgery, making book entry the way for investors to trade and transfer securities – and the ultimate proof of securities ownership.

So far, the model of the securities depository has shifted from direct holding to indirect holding and then returned to direct holding. There are two explanations for these shifts. First, the dematerialization of securities has largely reduced the cost of beneficial owner identification and post-trade processing. Second, with the further liberalization and integration of global financial markets, legal conflicts and regulatory dilemmas arising from nominal holding have become more prominent and a pressing problem for all relevant countries. For countries that developed securities markets rather late and do not have much experience with paper-form securities, how to use their "late mover advantage" wisely is an issue well worth studying.

The registration and depository system of the China interbank bond market (CIBM)

The rise of CIBM: In 1997, the People's Bank of China requested all commercial banks to open accounts with China Central Depository & Clearing Co., Ltd. (CCDC) for the depository of the securities they hold, which marked the formation of the CIBM[1]. Although the CIBM was a latecomer to the international financial arena, it met all the prerequisites to promote a book-entry securities system. Dematerialization, a challenging goal that took foreign markets more than a century to accomplish[2], was fulfilled in the CIBM in just a few years. Featuring a direct holding depository system facilitated by settlement agents, the CIBM has been operating smoothly for over two decades.

The direct holding system: Both the CIBM and the exchange market are based on the direct holding of securities by end investors: ie an institutional arrangement where beneficial owners of securities directly open accounts with a CSD. This differs from the indirect holding system, which involves a custodian bank functioning as the nominee account holder registered with a CSD on behalf of beneficial owners.

It should be noted that this article is not intended to address the advantages and disadvantages of the direct and indirect holding system, or to draw a conclusion to say which system is better. Even so, when it comes to the feasibility and suitability of a system which is to be introduced into another market, it is still necessary to evaluate how well one system can interact with the local environment. China's bond market, by leveraging its late mover advantage, completed dematerialization in a rather short period of time. Such a leap forward rendered the nominal account structure, which was created to facilitate the settlement and delivery of physical securities, no longer necessary.

Furthermore, the direct holding system effectively mitigated market risks arising from the lack of transparency of an indirect holding account structure. This was one of the hard lessons learned from the "327 China Government bond incident" and other similar experiences involving unauthorised speculation in the market[3]. In the "327 China Government bond incident", although the stock exchange at that time forbade its members to borrow securities from other members and put controls on its members' securities holding structures, such requirements were never fully met as a result of the obscure indirect holding account structure. After this painful event, the stock exchange decided to implement a direct holding system in the market.

The direct holding system clearly defines the legal relationship between the issuer and the investor, provides high-level protection for investors' rights and interests, accurately and rapidly reflects investors' securities and cash movements, and can monitor risks effectively. With fewer intermediaries involved, the direct holding system improves settlement efficiency, and eliminates the interdependencies between different layers in an indirect holding system. At the same time, settlement agents were introduced, providing value-added services for investors as custodians do in an indirect holding system. Such an arrangement not only protects investors, but also enhances post-trade efficiency.

Thoughts on aligning China bond market with international conventions

In July 2017, the northbound trading service of Hong Kong Bond Connect was officially launched. It is an important way to further open up China's bond market, and also an attempt to test the compatibility of the indirect holding system. The securities of investors participating in the CIBM via Hong Kong Bond Connect would all be deposited in the nominee account opened with CCDC by the Central Moneymarkets Unit of the Hong Kong Monetary Authority (CMU), which would itself be the registered owner for those securities. So far, Hong Kong Bond Connect has been operating steadily, but controversies over the recognition of beneficial

1. *Superpower Bond Market - Rise of the OTC Market,* Zhong Yan, *ChinaBond,* May 2017 issue.

2. According to the European *Central Securities Depositories Regulation*, all transferable securities (including existing and newly issued bonds) of member countries must become paperless by 1 January 2025.

3. The "327 incident" refers to the last day of trading for the 1995 March delivery government bond futures contract (27 March). As bond markets came under intense pressure due to runaway inflation, there had been significant, and often unauthorised, speculation on whether the Ministry of Finance would pay compensation to government bond holders, ultimately resulting in bankruptcies and indictments. This prompted a government ban on trading financial derivatives for several years.

owners' rights and interests under this scheme persist. The main reason behind this is the lack of effective alignment between the nominal holding structure commonly accepted by foreign markets and the regulatory system currently adopted by the CIBM.

Legislative considerations: The depth of legislation pertaining to the CIBM is generally low; and relevant legal documents in China have not yet set out any rules relating to the "nominee holder". "Nominal holding" is not a mere concept; rather, it should be a set of institutional rules that may affect the identification of property rights, transfer of securities, bona fide acquisition, bankruptcy protection, settlement and delivery obligations, etc. A concept not supported by actual legislation would leave investors in an awkward situation where they cannot find any legal basis for their claims.

Effectiveness of rights protection: Since a policy endorsed nominal holding system (in practice in the Bond Connect scheme) has not yet been effectively integrated into the current registration and depository system in the CIBM, proper protection for the rights and interests of end investors, once damaged, will be difficult to restore, as there is no applicable law to prove ownership and the procedures for obtaining evidence are complicated. For instance, in the determination of the preferential tax treatment for foreign institutional investors, if the end investor's tax residence cannot be identified with certainty due to the nominal holding arrangement, the investor may not be able to enjoy the correct preferential tax rates.

Regulatory requirements: With the intention of safeguarding the overall stability of the financial market, regulators carry out macroprudential supervision, and require relevant market institutions and financial market infrastructures to report to them in a transparent manner, namely to include statistics of settlements by sub-accounts and end investors all in their regulatory reports. In this kind of supervision, nominee account holders are actually the biggest obstacle; and the additional information report required seems very much redundant. This process will consume substantial human and material resources with little guarantee on the cost-effectiveness, timeliness and accuracy of regulation, which can actually be automatically avoided in the direct holding system due to its account structure arrangement. The direct holding system allows transparency of information automatically, thereby providing regulators with the most authentic and comprehensive market data.

As foreign investors quicken their pace to access the CIBM, CCDC has gradually developed the "ChinaBond Solution". This is a pragmatic integration of the direct holding account structure and the services provided by custodian banks to their clients.

The ChinaBond Solution, while adhering to the principle of registering beneficial ownership of securities directly with a CSD, takes into account the service relationships and interest distribution patterns in an indirect holding system. Especially, based on their close relationship with clients, custodians can provide better customized services to each client in the account opening, cash clearing and corporate action processes. For example, they can make the opening of a segregated security account in the local CSD much easier for the client; and they can provide better and more value-added services such as secured lines of credit and pre-advise of entitlements, etc.

The solution satisfies the market's legal and regulatory requirements, protects the rights and interests of beneficial owners without any change to the current operational habits of foreign investors, and will help build efficient inter-connectivity between the CIBM and global markets. The ChinaBond Solution, if implemented successfully, will effectively align China's bond market with international conventions. In this way, a cross-border registration and depository system with greater compatibility and better service scalability will be established, which will in turn help China's bond market open up further and develop steadily.

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Green, Social and Sustainability Bond Markets

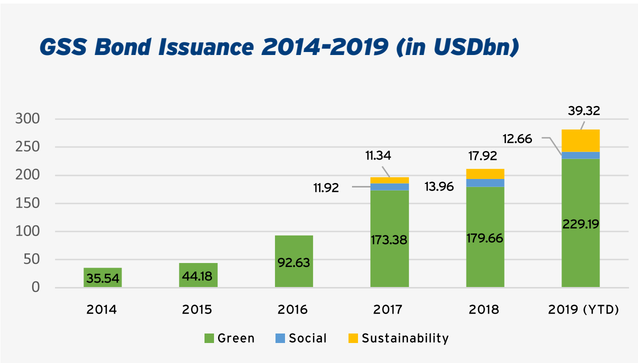


by Nicholas Pfaff, Valérie Guillaumin and Ozgur Altun

SF Green, social and sustainability bond market developments

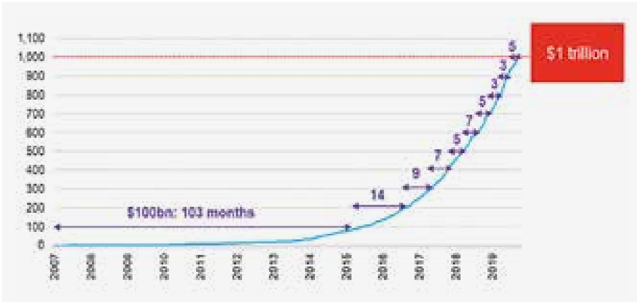
GSS bond issuance in 2019

Green, social and sustainability (GSS) bond issuance has continued to surge globally in 2019 reaching a total of USD281 billion as of 9 December 2019 and representing a 33% increase over 2018's total figure. Green bond (GB) issuance alone amounted to USD230 billion, bringing the total outstanding to date to over USD730 billion. Sustainability bond issuance has more than doubled year-on-year while social bond issuance is on track with the figure for 2018.



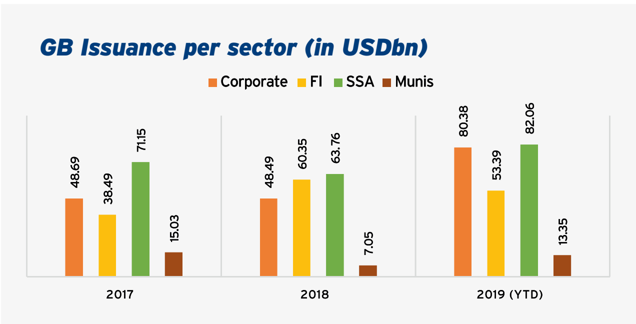
Source: ICMA based on Environmental Finance database (as on 09.12.2019)

On a more general basis, the cumulative sustainable debt issuance passed the USD1 trillion benchmark in October 2019 with sustainability-linked loans being an important contributor to this total. Also, while sustainable debt issuance took 103 months to hit the cumulative number of USD100 billion for the first time in 2015, the current issuance pace since 2018 now means that this figure is reached every five months on average (Source: Bloomberg NEF).



Source: Bloomberg NEF

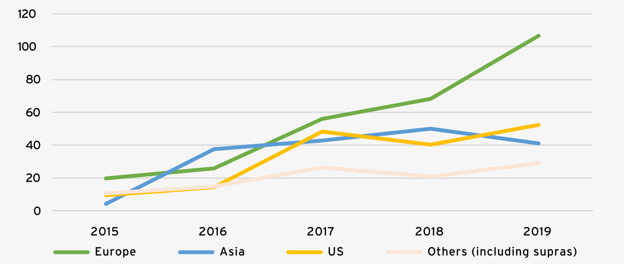
From the issuer type perspective, GB issuance from corporates and SSAs has increased substantially year-on-year, with nearly 67% and 29% respectively. Issuance from FIs is on track with 2018. 2019 has seen the first telecommunication sector company, Telefonica, joining the market with a EUR1 billion 5 year GB as well as EUR250 million sustainability bond from Otto, the German textiles, apparel and houseware retailer, representing the first from its sector. Also, in 2019, the Netherlands issued a EUR5.98 billion 21 year GB, which represents the first from a triple-A rated sovereign GB.



Source: ICMA based on Environmental Finance database (as on 09.12.2019)

Regionally, GB issuances from Europe (USD106.63 billion) and the US (USD52.35 billion) have seen a considerable increase in volume, ie by 56% and 30% year-on-year, respectively.

GSS Issuance per region (in USDbn)

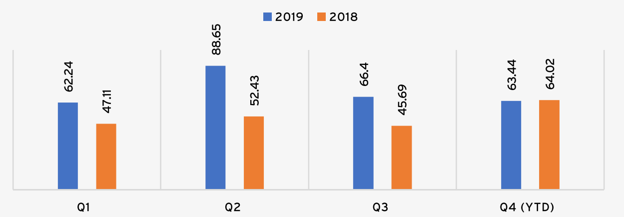


Source: ICMA based on Environmental Finance database (as on 09.12.2019)

GSS bond issuance in Q4 2019

Green, social and sustainability (GSS) bond issuance in Q4 2019 reached to a total of USD63.44 billion. GB issuance alone amounted to USD48 billion of this total.

GSS Bond Issuance 2014-2019 (in USDbn)



Source: ICMA based on Environmental Finance database (as on 09.12.2019)

- *Corporates:* GB issuance from corporates totalled USD17.43 billion in Q4 2019 seeing a year-on-year increase of 42.5%. The notable issuances included:
  - in October 2019, the inaugural GB issuance by PepsiCo (USD1 billion 30 year / use of proceeds: sustainable plastics and packaging, decarbonization of operations and supply chain, water sustainability, etc.); the inaugural issuance by CPI Property Group (EUR750 million 7.5 year / use of proceeds: Green Buildings, Energy Efficiency, Renewable Energy, etc.) representing the first issuance from the CEE region; and the return of E.ON to the market with its second GB issuance of EUR1.5 billion (Source: EF);
  - in November 2019, Apple's return to the market with EUR2 billion (in two tranches – EUR1 billion 6 year and EUR1 billion 12 year / use of proceeds: energy efficiency, renewable energy, terrestrial and aquatic biodiversity conservation, eco-efficient products production technologies and processes); the first issuance from a Ukrainian entity, DTEK Renewables, with a EUR325 million 5 year GB as well as JPY100 billion (USD920 million equivalent) GB issuance by Nidec Corporation, a Japanese electronic motors manufacturer; and
  - in December 2019, the first issuance from a mining company (SEK2 billion 10 year), Swedish state-run Luossavaara-Kiirunavaara, where proceeds will finance projects for transitioning from carbon-intensive iron ore extraction process to fossil fuel-free iron ore mining and steel production and electrifying its infrastructure (Source: EF).
  - Also, Engie (EUR900 million 11 year) and Orsted (EUR600 million and TWD12 billon) were among the biggest repeat contributors to the quarter's numbers.
- *Financial institutions (FIs):* GB issuance from FIs totalled USD14.23 billion in Q4 2019. The quarter's important issuances, among others, were Banco Santander's inaugural GB of EUR1 billion 7 year (use of proceeds: Renewable Energy), Bank of America's GB of USD2 billion 6 year, Crédit Agricole Group's return to the market with its second GB of EUR1 billion 5 year, all in October. Also in October, Assicurazioni Generali, the Italian Insurance Company, issued its inaugural (EUR 750 million 11 year) GB and became the first European insurance company to issue a GB. Issuances from China totalled USD3.6 billion, to which Bank of China and China Development Bank contributed with issuances of USD equivalent of USD963 million and USD1.42 billion respectively.
- *SSAs:* GB issuance figure reached a total of USD15 billion. Issuances from the Republic of Ireland (EUR2 billion 12 year in October), KfW (EUR1 billion 8 year in November and NOK2 billion 4 year in October), EIB and Kommuninvest (each USD1 billion, in October and November respectively), and Asian Development Bank (GBs of EUR750 million 10 year and GBP250 million 7 year in October) contributed greatly to this figure. Islamic Development Bank issued its inaugural green sukuk of EUR1 billion 5 year also in November. In September, EBRD issued two new thematic GBs, ie its inaugural "Climate Resilience Bond" (USD700 million 5 year) and "Green Transition Bond" (EUR500 million 5 year). The proceeds are exclusively earmarked for projects of climate-resilient infrastructure, climate resilient business and commercial operations, climate resilient agricultural and ecological systems, in the case of the former, and financing decarbonisation and resource efficiency projects, in the case of the latter.
- *Social and sustainability bonds:* Lastly, social and

Green, social and sustainability (GSS) bond issuance has continued to surge globally reaching a total of USD281 billion in December 2019.

sustainability bond issuance over the last quarter totalled USD15.36 billion while the quarter has seen important players joining the market. In October, OKB (EUR500 million 7 year), Action Logement Services (EUR1 billion 15 year) and Bank of Montreal (USD500 million 3 year) issued their inaugural sustainable bonds. Also, in October, the Development Bank of Japan returned to the market with a new USD 1 billion 5 year sustainability bond. In November, RBS issued its inaugural social bond of EUR750 million 6 year (use of proceeds: employment generation including through the potential effect of SME financing and microfinance); and Land NRW issued a two tranche (EUR1 billion 10 year and EUR1.5 billion 20 year) sustainability bond. Also, in November, DKB issued the first so-called "Blue covered bond" (EUR500 million) that will finance public water and waste management facilities; and ANZ Bank from Australia issued the first EUR SDG Tier 2 bond (EUR1 billion 10 year).

Notable market transactions

In September 2019, an innovative structure was successfully introduced to the market – the Enel USD1.5 billion 5 year SDG-linked bond with a step-up feature. The trigger for the one-time 25 basis points step-up coupon is dependent on Enel achieving its target of renewable energy installed capacity equaling or exceeding 55% total installed capacity by the end of 2021 departing from 45.9% in June 2019.

In November 2019, CA-CIB issued a EUR100 million 10 year "Transition Bond" subscribed by AXA IM in the form of a private placement. The bond is listed on the Luxembourg Stock Exchange. The proceeds of the bond will be earmarked by CA-CIB to a selection of loans made to projects in carbon intensive sectors which contribute to the transition to a low carbon economy, such as LNG-powered ships, investments in energy efficient industries as well as gas power assets in countries where power generation currently relies on coal.

As for background to this transaction, in June 2019, AXA IM had called for a new thematic bond distinct from green bonds and published a first proposal for guiding principles. These "Transition Bonds" were proposed for finance the transition of carbon-intensive sectors/companies towards a low carbon society. In October, the GBP SBP Executive Committee decided in Washington to set up a Climate Transition Finance Working Group with the mandate to understand why corporate issuers from carbon intensive industries have been largely absent from the green bond market thus far and to consider providing guidance for potential future issuances.

Recent initiatives from Stock Exchanges

In October 2019, LSE launched its Sustainable Bond Market segment, bringing together its green bond segment (launched in 2015) with new dedicated segments for social and sustainability bonds as well as the newly-created issuer-level segment for bonds by issuers whose core business is aligned with the green economy, subject to a minimum 90% "green revenues" requirement in line with FTSE Russell's Green Revenues Taxonomy.

In November 2019, Euronext announced the creation of a new Euronext Green Bonds offering which brings together green bonds from six regulated markets in one dedicated section on the Euronext website. In order to be eligible for inclusion in the list, green bonds must be listed on a Euronext market, be aligned with recognizable industry standards such as ICMA Green Bond Principles or the Climate Bond Initiative Taxonomy, and be accompanied by an appropriate external review performed by an independent third party.

In December 2019, Nasdaq announced the launch of the Nasdaq Sustainable Bond Network which aims to increase transparency and accessibility to environmental, social and sustainability bonds globally. It enhances Nasdaq's Sustainable Bonds Market, launched in 2015, with respect to the sustainable bonds' investment process, allowing investors to source detailed information on sustainable bonds for product due diligence, selection and monitoring based from a centralized and open platform.

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European Action Plan on Sustainable Finance

Background

SF The European Commission established the Technical Working Group on Sustainable Finance (TEG) in June 2018 following the publication in March 2018 of the Action Plan on Sustainable Finance. ICMA, with the support of the GBP SBP Executive Committee, was nominated on the TEG following a highly selective process. The TEG published on 18 June 2019 reports and guidelines relating to its four key deliverables (see here) on which ICMA has provided a summary review with comments. The TEG's mandate has now been extended until mid-2020 and it will continue its work especially with respect to the Taxonomy and the EU Green Bond Standard.

This article reviews the status of the TEG workstreams with ICMA's perspective, and provides an update on the parallel EU legislative initiatives on sustainable finance (see Table 1) that are under way reflecting the Commission's legislative proposals of May 2018. It focuses especially on the implications of the political agreement on the Taxonomy Regulation reached on 18 December 2019 by the European Council and the European Parliament.

Political agreement on the Taxonomy Regulation

After the publication of its Action Plan on sustainable finance, the European Commission launched in spring 2018 dual initiatives to develop an EU Taxonomy for sustainable activities. On the legislative front, this took the form of a proposal for a Regulation on the establishment of a framework to facilitate sustainable investment (the "Taxonomy Regulation"). This Regulation establishes the conditions and the framework to gradually create a unified classification system ("Taxonomy") on what can be considered an environmentally sustainable economic activity. In parallel, it tasked the TEG to develop as a priority the technical details of the Taxonomy. The TEG report on the EU Taxonomy for sustainable activities published in July 2019 sets out the basis for a future EU Taxonomy and aims to help investors and other potential users to start to understand the implications of the Taxonomy.

On 18 December 2019, the European Council and the European Parliament reached a political agreement on the Taxonomy Regulation. The Taxonomy Regulation will introduce a complex classification system of sustainable activities based on contributions to environmental objectives and technical criteria, as well as wider social and sustainability factors. It also recognises transition and enabling activities. The Taxonomy Regulation will not only apply to sustainable financial products, but also stipulates mandatory disclaimers for mainstream fund and pension products that are not using the Taxonomy as well as reporting requirements for large firms already subject to the Non-Financial Reporting Directive. These latter corporate level disclosures may however facilitate those required of financial intermediaries by the separate and earlier Disclosure Regulation. The Taxonomy Regulation will start applying from December 2021 (initially, with respect to the climate change mitigation and adaption activities) and is likely a landmark Regulation that requires the attention of all capital market participants and stakeholders in Europe and internationally.

A complex classification framework

The Taxonomy Regulation provides for a general framework that will allow for the progressive development of an EU-wide classification system for environmentally sustainable economic activities. This framework has however gained in complexity as it expanded to incorporate wide sustainability criteria and climate transition.

The Taxonomy Regulation sets out six environmental objectives: (i) Climate Change Mitigation, (ii) Climate Change Adaptation, (iii) Sustainable Use and Protection of Water and Marine Resources, (iv) Transition to a Circular Economy, (v) Pollution Prevention and Control and (vi) Protection and Restoration of Biodiversity and Ecosystems. It also includes four requirements that economic activities need to comply with in order to qualify which are that (i) they provide a substantial contribution to at least one of the six environmental objectives above, (ii) "No significant harm" is caused to any of the other environmental objectives, (iii) compliance with robust and science-based technical screening criteria, and (iv) compliance with minimum social and governance safeguards.

The Taxonomy recognises three further different types of environmentally sustainable economic activities:

- *sustainable activities* that in and of themselves contribute substantially to one of the six environmental objectives;
- *transition activities* for which there are no technologically and economically feasible low carbon alternatives, but that support the transition to a climate-neutral economy in a manner that is consistent with a pathway to limit the temperature increase to 1.5 degrees Celsius above pre-industrial levels, for example by phasing out greenhouse gas emissions;
- *enabling activities* that enable others to make a substantial contribution to one or more of the objectives, and where that activity does not lead to a lock-in of assets that undermine long-term environmental goals, and considering the economic

lifetime of those assets has a substantial positive environmental impact on the basis of life-cycle considerations.

Nuclear energy is neither explicitly excluded nor included in the list of eligible environmentally sustainable economic activities. The importance of "climate-neutral energy" for the transition has been explicitly recognised in a recital. The decision to include or exclude nuclear energy has been left to the detailed rules based on technical expert input, subject to "do no significant harm criteria", in particular with regards to the disposal of waste, as well as specific references to life-cycle considerations. Gas is also neither included nor excluded from the EU taxonomy. It will be subject to a technical assessment for the development of the delegated legislation.

Finally, the Taxonomy Regulation creates a review clause which would allow the Commission to investigate extension of the Taxonomy to activities which cause significant harm to environmental objectives ("brown taxonomy").

A mandatory reference for sustainable financial products

Once the Taxonomy Regulation is implemented, it will become a mandatory reference for sustainable financial products in Europe, and specifically:

- Funds and pension products as defined in the Regulation[1] will need to disclose how and to what extent their underlying investments support economic activities that meet all the criteria for environmental sustainability under the Taxonomy Regulation.
- The Taxonomy Regulation will need to be used by Member States or the European Union when they say that public measures, standards or labels concerning financial products or corporate bonds offered by financial market participants or issuers are environmentally sustainable.
- Future European labelled sustainable financial products such as the European Green Bond Standard or the Ecolabel for Financial Products are respectively expected to be totally and partially aligned with the Taxonomy.

A significant extension of sustainability disclosure requirements

The Taxonomy Regulation significantly expands the scope of sustainability disclosures as it will impact both mainstream funds and pension products and introduce new reporting requirements for large organisations:

- Mainstream funds and pension products that do not propose to specifically invest in sustainable activities will need to make an explicit statement that their investments do not take into account the Taxonomy Regulation.
- Financial and non-financial companies that fall under the scope of the Non-Financial Reporting Directive (NFRD) would have to disclose information on how and to what extent their activities are associated with environmentally sustainable economic activities. This refers to large public-interest companies with more than 500 employees, covering approximately 6,000 companies and groups across the EU.

These latter issuer-level disclosures may facilitate those required of firms that are subject to the Disclosure Regulation. This Regulation lays down rules for financial market participants (FMPs)[2] and financial advisers on transparency for the integration of sustainability risks and the consideration of adverse sustainability impacts in their processes, as well as the provision of sustainability-related information notably with respect to funds and pension products.

Implementation and timelines

The Taxonomy will be developed through delegated acts and will be published in two sequences. Specifically:

- The delegated act on the first two climate-related objectives (ie "Climate Change Mitigation" and "Climate Change Adaptation") should be adopted by the Commission by 31 December 2020 and will start applying as of 31 December 2021.
- The delegated act on the remaining four environmental objectives should be adopted by the Commission by 31 December 2021 and will start applying as of 31 December 2022.

1. These funds and pension products are referred to as "financial products" and are defined as: (a) a portfolio managed in accordance with mandates given by clients on a discretionary client-by-client basis where such portfolios include one or more financial instruments (b) an alternative investment fund (AIF); (c) an insurance-based investment product (IBIP); (d) a pension product; (e) a pension scheme; (f) an undertaking for collective investment in transferable securities (UCITS); or (g) a pan-European personal pension product (PEPP).

2. Article 2(1) of the Disclosure Regulation defines "financial market participants" as: (a) an insurance undertaking which makes available an IBIP; (b) an investment firm which provides portfolio management; (c) an institution for occupational retirement provision (IORP); (d) a manufacturer of a pension product; (e) AIF manager; (f) a PEPP provider; (g) a manager of a qualifying venture capital fund registered in accordance with Article 14 of Regulation (EU) No 345/2013; (h) a manager of a qualifying social entrepreneurship fund registered in accordance with Article 15 of Regulation (EU) No 346/2013; (i) a management company of UCITS; or, a credit institution which provides portfolio management.

Further development of technical criteria

The TEG recommendations are the first input to the Commission's work on developing the future delegated acts. The TEG will finalise its recommendations by February 2020.

A Platform for Sustainable Finance gathering various experts and stakeholders will be created to assist the Commission in the development of these delegated acts. It will be tasked with providing advice on the technical screening criteria and a number of other relevant topics. The Commission will also be advised by a Member State Expert Group to ensure the suitability and usability of the criteria.

Other TEG workstreams

Concerning the EU Green Bond Standard (EU GBS), the TEG is working on the implementation parameters of its proposal for the accreditation of external verifiers and also considering guidance for the practical use of the Taxonomy for future EU GBS issuers. As a reminder, the report on the EU GBS proposes that the Commission creates a voluntary, non-legislative EU Green Bond Standard. It requires (i) alignment with EU Taxonomy, (ii) publication by the issuer of a Green Bond Framework confirming among other things the voluntary alignment of green bonds issued with the EU GBS, (iii) mandatory reporting on use of proceeds (allocation report) and on environmental impact (impact report), and (iv) mandatory verification of the Green Bond Framework and of the allocation report by an external reviewer.

Following an analysis of the responses received from the related call for feedback during the summer, and amendments to the report where appropriate, the TEG published the final version of the report on *EU Climate Benchmarks and Benchmarks' ESG Disclosures* on 30 September 2019. This report will serve as a basis to the drafting of delegated acts by the Commission in accordance with the empowerments contained in the amending benchmark Regulation. The draft delegated act will be subject to a formal four-week public consultation by the Commission. The draft delegated acts are expected to be adopted early in 2020.

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Table 1: Update on EU legislative and regulatory initiatives on Sustainable Finance

Initiative	Current Status	Comments
Taxonomy Regulation	On 18 December.2019, EP and the Council reached a political agreement on the Taxonomy Regulation.	In December 2019, EP and the Council reached a political agreement on the compromise text for the Taxonomy Regulation. This regulation sets out six environmental objectives: (i) climate change mitigation, (ii) climate change adaptation, (iii) sustainable use and protection of water and marine resources, (iv) transition to a circular economy, (v) pollution prevention and control, and (vi) protection and restoration of biodiversity and ecosystems. It provides for four core requirements that economic activities should comply with in order to qualify: (a) substantial contribution to at least one of the above objectives, (b) doing no significant harm to any other of the objectives, (c) compliance with robust and science-based technical screening criteria, and (d) compliance with the minimum social and governance safeguards. It applies to: • MSs and the EU, when setting out any requirements on FMPs or issuers in respect of financial products or corporate bonds that are made available as environmentally sustainable; • FMPs offering financial products[3], which will be required to (i) disclose how and to what extent investments underlying the offered financial products support economic activities that comply with the criteria of the Taxonomy Regulation and (ii) to make a statement that the relevant investments do not take into account the Taxonomy Regulation in cases where products do not invest in taxonomy-compliant activities; and • Financial and non-financial companies that fall under the scope of the Non-Financial Reporting Directive (NFRD) will have to disclose information on how and to what extent their activities are associated with environmentally sustainable economic activities. This refers to large public-interest companies with more than 500 employees, covering approximately 6,000 companies and groups across the EU. The Taxonomy will be developed through delegated acts and will be published in two sequences. Specifically: • The delegated act on the first two climate-related objectives (ie "Climate Change Mitigation" and "Climate Change Adaptation") should be adopted by the Commission by 31 December 2020 and will therefore start applying as of 31 December 2021. • The delegated act on the remaining four environmental objectives should be adopted by the Commission by 31 December 2021 and will therefore start applying as of 31 December 2022.
Disclosure Regulation (2019/2088)	Regulation 2019/2088 of 27 November 2019 on sustainability-related disclosures in the financial services sector was published in the OJ L 317, 9 December.2019, pages.1-16 and will apply as from 21 March 2021.	The Disclosure Regulation lays down harmonised rules for FMPs and financial advisers on transparency with regard to the integration of sustainability risks and the consideration of adverse sustainability impacts in their processes and the provision of sustainability-related information with respect to financial products. It applies to (among others); investment firms and credit institutions providing portfolio management, AIFM, UCITS management companies, defined as FMPs, as well as financial advisers. The Disclosure Regulation provides various obligations for FMPs and/or financial advisers to ensure transparency on: (i) sustainability risk policies in investment decision-making or advice processes, (ii) adverse sustainability impacts of investment decisions at entity level, (iii) remuneration policies in relation to the integration of sustainability risks, (iv) the integration of sustainability risks in pre-contractual disclosures, (v) adverse sustainability impacts at financial product level, (vi) the promotion of environmental or social characteristics in pre-contractual disclosures, (vii) sustainable investments in pre-contractual disclosures, (viii) the promotion of environmental and social characteristics and of sustainable investments on websites and periodic reports. The technical standards for public disclosure of principal adverse impacts of investment decisions and product specific disclosures will be developed by ESMA.

3. Article 2(12) of the Disclosure Regulation defines "financial product" as: (a) a portfolio managed in accordance with mandates given by clients on a discretionary client-by-client basis where such portfolios include one or more financial instruments; (b) an alternative investment fund (AIF); (c) an IBIP; (d) a pension product; (e) a pension scheme; (f) a UCITS; or (g) a PEPP.

Initiative	Current Status	Comments
Amendments to BMR (2016/2341)	Reg. (EU) 2019/2089 of 27 November 2019 amending Reg. 2016/1010 (BMR) as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks ("the Amending Regulation") was published in the OJ L 317, 9 December.2019, pages 17-27 and entered into force on 10 December.2019.	The Amending Regulation introduces two new benchmarks: (i) "EU Climate Transition Benchmark" ("EU CTB") where the underlying portfolio follows a measurable, science-based and time-bound trajectory towards alignment with the objectives of the Paris Agreement (so-called "decarbonization trajectory"); and (ii) "EU Paris-aligned Benchmark" ("EU PAB") where the resulting benchmark portfolio is aligned with the objectives of the Paris Agreement. The applicable minimum standards (including the criteria for the choice and the weighting of underlying assets as well as the determination of the decarbonization trajectory for EU CTB) will be established by delegated acts, with the input of the TEG's recommendations, and will require compliance by the provider of such benchmarks with the Amending Regulation by 30 April 2020. Accordingly, administrators of EU CTB and EU PAB (as well as significant equity and bond benchmarks) will disclose information on their overall alignment with the Paris Agreement pursuant to Article 9(3) of the Disclosure Regulation in their benchmark statements by the same date. Apart from the introduction of these new two benchmarks, the Amending Regulation provides various obligations on administrators of the benchmarks subject to BMR, such as the obligation to publish an explanation of how the key elements of the benchmark methodology reflect ESG factors and to contain in the benchmark statement an explanation of how ESG factors are reflected (in the case of the benchmark not pursuing or taking into account any ESG objectives/factors, to include a clear benchmark statement thereof) by 30 April 2020. By 31 December 2021, for each benchmark or family of benchmarks (except interest rate and foreign exchange benchmarks), there will be an obligation to disclose in the benchmark statements an explanation of how their methodology aligns with the target of carbon emission reductions or attains the objectives of the Paris Agreement.
Various Delegated Acts and Amendments to respective ESMA guidelines	ESMA and EIOPA published their final reports in response to EC's request (on 24 July 2018) for technical advice on 30 April.2019. ESMA's technical advice on the integration of sustainability considerations in credit ratings was published on 18 July 2019.	EIOPA and ESMA published their final reports in response to the technical advice on sustainability of the European Commission on 30 April 2019. ESMA recommended amending relevant requirements to ask all UCITS management companies and AIFMs to consider sustainability risks in their internal processes, systems and controls, devote sufficient resources to the integration of sustainability risks; and ensure that senior management is responsible for the integration of sustainability risks. On the MiFID II front, similarly, ESMA recommended ESG considerations to be integrated in general organizational requirements risk management policies and procedures of firms in scope. Also, ESMA proposed that investment firms should disclose potential conflicts of interest that may stem from the distribution of sustainable investments and that manufacturers and distributors should be required to consider clients' ESG preferences within the target market of investment products and within the mandatory product review process. ESMA's technical advice on sustainability considerations in the credit rating market and its final guidelines on disclosure requirements applicable to credit ratings were published on 18 July 2019. As for the technical advice, ESMA found that while credit rating agencies (CRAs) are considering ESG factors in their ratings, the extent of their consideration can vary significantly across asset classes, according to each CRA's methodology. ESMA also concluded that it would be inadvisable to amend the CRA Regulation to explicitly mandate the consideration of sustainability characteristics in all rating assessments given the specific role that credit ratings have in the EU regulatory framework. Instead, ESMA proposes that the European Commission assesses whether there are sufficient regulatory safeguards in place for other products that will meet the demand for pure sustainability assessments. Secondly, ESMA developed guidelines to improve the quality and consistency of the information accompanying credit rating actions including a requirement of greater transparency around whether ESG factors were a key driver of the credit rating action.

Asia Pacific SDG/ESG survey: overview and key takeaways

By Keiko Nakada, Japan Securities Dealers Association (JSDA) and Secretariat, Asia Securities Forum (ASF)

SF ICMA and Japan Securities Dealers Association (JSDA) have enjoyed a long and productive relationship, which recently has extended to cooperation on sustainable finance - in particular collaborating to promote fundraising for environmental and social projects through the green, social and sustainability bond markets. ICMA and JSDA have held three successful conferences on developments in the green and social bond markets in Tokyo, the most recent in October last year featuring a speech from Japan's Minister of the Environment, Shinjiro Koizumi. In addition, the UN Sustainable Development Goals (SDGs) are an area of common interest for ICMA and JSDA. The Green Bond Principles promoted by ICMA provide a mapping from its Green Project Categories to the SDGs by which issuers, investors and bond market participants can evaluate the financing objectives of a given green, social or sustainability bond in the context of the SDGs and related targets. JSDA has also undertaken various initiatives related to the SDGs and recognizes the achievement of sustainability as imperative for not only the Japanese securities market it represents but also the world at large. Both organisations' initiatives in this arena underscore a global trend where sustainability and the SDGs have become a topic of high priority.

ASF's initiatives to promote the SDGs: The Asia-Pacific region comprises more than half of the world's population, attains and sustains rapid economic growth, and plays an invaluable role in driving the world economy. However, it also houses about 52% of the world's poorest people, and with rapid industrialization and changes to social structure, many jurisdictions face difficult social and environmental challenges.

Given the strategic and economic importance of the region, addressing its social, economic, and environmental problems would be a large step for the project of global sustainability and would also greatly contribute towards the achievement of the SDGs.

Against this backdrop, the Asia Securities Forum (ASF), a consortium of 25 national and regional organizations in the securities industry from across the Asia-Pacific region, adopted the Bali Declaration on Promotion of SDGs at its 2018 Annual General Meeting held in Bali, demonstrating its commitment to the achievement of the SDGs and resolve to further the efforts of ASF members in this arena. The JSDA serves as Secretariat to the ASF, and ICMA's Asia Pacific Representative Office is an ASF member.

In line with the spirit of the Bali Declaration, the ASF's new Working Group for Promotion of SDGs (WG) launched its first major activity: a survey on SDG/ESG-related matters and on the status of sustainable finance in the ASF member jurisdictions.

The motivations behind the survey were that, despite the rapid rise of ESG investment—a major area in which the financial/securities industry can effectively contribute to the SDGs—there is also a lack of comprehensive data and information about ESG financing within the Asia-Pacific region. To serve as a first step in remedying this, the WG decided to begin by collecting information on ESG investment in the region in a manner that could be compared across borders.

The results of the survey, along with the full text of all of the responses and additional materials provided by respondents, are currently available on the ASF website. Respondents included 15 organisations (representing 14 jurisdictions), along with ICMA.[4] The information collected was as of the end of 2018.

Government policies and initiatives to support sustainable finance: The survey sought to capture the basic regulatory or policy framework in each jurisdiction. In terms of government policies/initiatives for sustainable finance, the most commonly introduced form of initiative was that of standards or guidelines (9 out of 14 jurisdictions) rather than regulation (8 out of 14).

The standards/guidelines included those pertaining to financial products and services such as green bonds and SRI funds, corporate governance and stewardship/investment governance, and also initiatives for Islamic finance through the SRI Sukuk Framework.

Entities committed to sustainable finance initiative: Amongst the entities supporting sustainable finance, exchanges (14 jurisdictions) and industry associations (13 jurisdictions) stood out in terms of their contributions to this end. Every respondent jurisdiction's exchange was a signatory to the Sustainable Stock Exchanges Initiative (SSE). Industry associations were not limited to securities associations but also included bankers' associations, investment or fund associations, corporate governance associations, responsible investment associations, and business associations.

Characteristics for each asset class: The survey also looked into the market size and characteristics for each asset class. The results indicated that the market sizes vary considerably depending on the stage of ESG market development in each jurisdiction.

Looking at the bond markets, green and social bonds were issued in 13 jurisdictions as the most commonly adopted means of sustainable finance. These included Australia, China, Chinese Taipei, India, Japan, Korea, Malaysia, Mongolia, New Zealand, Russia, Singapore, Thailand, and Turkey.

4. Respondents to the survey are as follows: Australian Financial Markets Association (AFMA), Securities Association of China (SAC), Chinese Taiwan Securities Association (CTSA), Bombay Stock Exchange Brokers' Forum (BBF), Japan Securities Dealers Association (JSDA), Korea Financial Investment Association (KOFIA), Association of Stockbroking Companies Malaysia (ASCM), Mongolian Association of Securities Dealers (MASD), New Zealand Financial Markets Association Inc. (NZFMA), Russia National Finance Association (NFA), Securities Association of Singapore (SAS), Association of Thai Securities Companies (ASCO), The Thai Bond Market Association (ThaiBMA), Turkish Capital Markets Association (TCMA), Vietnam Association of Securities Business (VASB) (15 organizations from 14 jurisdictions) and ICMA Asia Pacific Representative Office (global organization).

In the equity markets, disclosure of non-financial information or climate risks was the most commonly observed practice (seen in 12 jurisdictions). While there were a few advanced cases, the requirement remains partial or on a voluntary basis in most jurisdictions.

In addition, there existed ESG-related indexes in 9 jurisdictions. Such indexes were typically issued by exchanges or global rating agencies focusing on specific region or jurisdiction, with focus on diverse areas related to ESG, including carbon efficiency, fossil fuel free, new energy, and corporate governance. ETFs referring to ESG indexes also existed in some jurisdictions.

ESG-themed funds were also common (12 jurisdictions). Various types of funds, including private equity funds, investment trust funds, pension funds, ESG investment company funds were found to be prominent in the region.

Sustainable Investors: Public or non-public pension funds and retirement funds, or signatories to investors' codes that support sustainable finance were found to be the most prevalent sustainable investors of the region. In particular, there were a significant number of signatories to global initiatives (such as the PRI and UNEP FI) by fund managers and financial institutions, representing an awareness and commitment within the region to the goals set by such initiatives.

Next steps: The ASF Secretariat reported the results of the survey at the ASF Annual General Meeting 2019 held in November in Istanbul. The ASF also launched an ASF webpage dedicated to the SDGs with the aim of providing a tool for all ASF members and stakeholders to share relevant information. In addition, the ASF plans periodical updates to the survey post-2020. As an increasing number of global stakeholders are interested in sustainable finance, the ASF hopes that this report can be utilized as a reference point of information relevant to this arena specific to the Asia-Pacific region.

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Asset Management

by David Hiscock, Arthur Carabia and Bogdan Pop

Fund liquidity

CMU

In light of both market events and new regulatory developments in Europe, the AMIC Executive Committee along with EFAMA's Board of Directors decided, in July 2019, to update the report on fund liquidity which they jointly published in 2016 – in order to adjust it to today's context, without repealing the previous contribution made in 2016.

The updated report, which is due to be published early in 2020, shows that since 2016:

(1) The EU regulatory framework has been further enhanced as a result of important new policy developments, including:

- the EU *Regulation on Money Market Funds* (MMFs) (June 2017) and ESMA's *Guidelines on Stress Test Scenarios under the MMF Regulation* (July 2019): following the FSB's 2017 recommendations, Money Market Funds are now subject to dedicated regulation including, among others, stringent asset diversification and liquidity rules, and specific liquidity stress tests;
- ESMA's *Guidelines on Liquidity Stress Testing* (LST) in UCITS and AIFs (September 2019): following the 2017 FSB and ESRB recommendations, UCITS and AIFs, already subject to LST requirements under Level 1 and 2, will have to comply with ESMA guidelines which will converge and enhance LST practices;
- IOSCO's *Recommendations on Liquidity Risk Management for Collective Investment Schemes* (February 2018): this report shows that, following IOSCO's 2018 recommendations, several EU jurisdictions have decided to make liquidity management tools available or introduce new provisions at national level.

Following recent market events, the update also provided the opportunity to emphasize that the UCITS framework clearly states that there should be no presumption of liquidity for listed securities; and that it gives supervisors the opportunity to control where unlisted securities can be listed.

This purpose of this stock-taking exercise is to remind fund managers of their own duties, but it also provides an overview to supervisors and policy makers on what was accomplished at EU level over past decades. This part of the report will hopefully also be valuable in the context of IOSCO's 2020 review of its liquidity risk management recommendations for investment funds, which we support.

(2) This comprehensive framework has been tested across various market conditions and scenarios via a number of additional reports, including:

- ESMA's *Annual Statistical Report on EU Alternative Investment Funds* (March 2019): despite potential areas of vulnerability, this first AIFMD report shows that overall most AIFs do not have significant liquidity mismatches;
- ESMA's *Economic Report on Stress Simulation for Investment Funds* (September 2019): despite potential areas of vulnerability, this first sector-wide stress simulation (6,000 UCITS bond funds) highlights that "overall most funds are able to cope with such extreme but plausible shocks, as they have enough liquid assets to meet investors' redemption requests".

Our report welcomes these assessments and recalls that they do not take into account the potential mitigating

> **We note that, despite progress being made since 2016, LMT are not yet fully available across the EU.**

effects of liquidity risk management tools, as highlighted by IOSCO's reports on *Open-ended Fund Liquidity and Risk Management – Good Practices and Issues for Consideration* (February 2018) and on *Liquidity in Corporate Bond Markets Under Stressed Conditions* (June 2019).

(3) *Our previous recommendations are still valid and need to be expanded:*

- *Focus on supervision and enforcement of the current comprehensive EU rules:* After several years dedicated to the development of new rules, we believe the focus should now be on supervision and enforcement, which is instrumental to the framework's effectiveness. In this context, we support ESMA's intention to ensure, in 2020, an effective and consistent implementation of existing liquidity provisions contained in the UCITS Directive.
- *Make the full IOSCO suggested Liquidity Management Tools (LMT) available across the EU:* We note that, despite progress being made since 2016, LMT are not yet fully available across the EU. We therefore encourage ESMA to work with national authorities to allow fund managers to use LMT when appropriate and, in this context, we welcome IOSCO's 2020 review of liquidity risk management recommendations for investment funds.
- *Improve transparency and knowledge of end-investors to enhance liquidity stress tests and ease the management of potential redemption shocks:* For fund managers, the availability of data from distributors on underlying investors is a key challenge for conducting liquidity stress tests, which involves considering investor behaviour as required by ESMA LST Guidelines, adopted in September 2019. For the purpose of sound risk management, we believe that the communication of basic information to fund managers including at least investor profiles and shares/units held by these categories of underlying investors should be mandatory and free of charge.
- *Enhance market liquidity for corporate bonds and small and medium caps:* We are calling on the Commission to follow up on the policy recommendations of its expert group on corporate bonds and, in particular, to at least phase in the implementation of the mandatory buy-in regime under CSDR, which could significantly hinder market liquidity as shown by a recent study released by ICMA

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The IOSCO leverage recommendations

IOSCO published on 13 December 2019 its final recommendations to help regulators assess leverage in investment funds. AMIC had the opportunity to contribute to this proposal by issuing a paper, jointly with EFAMA, on the topic, in July 2017 and by answering to IOSCO's consultation, in February 2019.

The AMIC Risk Management Working Group will reconvene, early in 2020, to discuss in further detail the now proposed two-step approach, as follows:

Step 1 provides a single common approach to filter and select a sub-set of investment funds for further analysis.

As a baseline analytical tool, IOSCO recommends that regulators use the Gross Notional Exposure (GNE) or adjusted GNE (limiting overstatement of exposure to derivates and options) broken down by asset classes, and long and short exposures.

We note that the final recommendations allow regulators to exclude from scope funds which are unlikely to present leverage-related risks, as foreseen under AIFMD for funds not using leverage on a substantial basis (ie three times NAV), and which should also lead to exclusion at EU level of UCITS funds, which are even less leveraged (ie maximum 2.1 times NAV).

The reporting by asset class also seems to be compatible with the current reporting requirement under AIFMD, which already asks for a "breakdown of leverage arising from borrowing of cash or securities and leverage embedded in financial derivatives".

In line with AIFMD requirements, AMIC called in its response to the consultation to use instead the GNE approach combined with Net Exposure Measures (taking into account hedging and netting) as the first filter. We note however that under this recommendation the use of net exposure measures (accounting for netting and hedging) is only allowed as an optional approach.

Step 2 involves performing an analysis of identified funds based on risk-based measures and at the discretion of regulators.

IOSCO members have identified some leverage-related risk measures that are common across jurisdictions, which includes among others: (i) information regarding collateral management (cleared/uncleared, margin posted/received, re-hypothecation), borrowing and cash, assets available for liquidation in a day; (ii) data points to estimate the effects of changes in market factors (VaR, Beta, DV01); and (iii) other general information about the fund (strategy, size, counterparty exposures, investors profiles).

However, IOSCO recommends that each regulator determine its approach to define appropriate risk-based measures for analysing funds identified under Step 1 which may potentially pose significant leverage related risks to the financial system. It therefore remains to be seen if these could have an impact at EU level.

Finally, as next a step, IOSCO will publish an annual report reflecting leverage trends within the asset management industry at a global level, based on GNE or adjusted GNE aggregated by asset class, including long and short exposures for funds assessed under Step 1. The first report is scheduled to be published in 2021. In this context we note that IOSCO highlights in its report how the GNE and adjusted GNE can misrepresent leverage and a fund's market footprint and therefore hope this report will clearly state that these funds do not necessarily pose a risk to financial stability.

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ELTIFs

CMU

The ELTIFs Regulation, which entered into application on 9 December 2015 and was the creation of a new brand of fund available for both retail and professional investors to invest in long-term assets, is now under review. Despite a favourable political context (ie the Investment Plan for Europe and Capital Markets Union) and the fact that the industry had welcomed this initiative, only a very limited number of ELTIFs had been launched so far. In the context of the review of the founding Regulation and the relaunch of the CMU project, AMIC finalised a position paper on the topic.

While remaining respectful of the need to provide the right degree of control to satisfy legitimate concerns, such as investor protection, AMIC makes four recommendations in order to facilitate the take-up of ELTIFs and significantly boost their contribution towards the financing of much needed longer-term investment:

(1) to widen the list of eligible assets by: (a) clarifying the definition of real assets; (b) raising the threshold of market capitalisation of qualifying portfolio undertaking; and (c) extending the possibility to invest in other collective investment undertakings, like AIFs that exclusively invest in eligible assets;

(2) to align the encumbrances limit with market practice: the current limit seems to have been set in order to be in line with the 30% limits applied to the borrowing of cash, but this needs to be raised significantly as it is market practice for lenders to require security that exceeds the amount borrowed – in order to better manage credit risk;

(3) to simplify requirements regarding eligible investors: given the diversification rules and the retail distribution requirements which are already in place to protect retail investors, it would be appropriate to delete the mandatory minimum entry ticket and amend the 10% investment limit. It would also be helpful to streamline suitability test requirements and avoid duplications (as currently both MIFID and ELTIF apply). In the case of institutional investors detailed proportion of portfolio composition and diversification rules with strict limits are counterproductive and should be deleted;

(4) to tackle tax treatment issues: by creating a new harmonised fund structure, the Commission hoped to ensure that ELTIFs display a coherent and stable product profile for investors to invest in; but several national considerations, not least among which is tax, continue to impinge on this. AMIC realizes that addressing tax issues, which require a unanimous decision from Member States, could considerably slow down the review which should rather be a quick fix exercise. We therefore suggest prioritizing points 1 to 3 and addressing point 4 once/if circumstances allow it.

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The ESAs' review of PRIIPS: the buy-side view

CMU

AMIC will submit, on 13 January 2020, its response to the ESAs consultation on the review of the regulatory technical standards (RTS) of the Key Information Document (KID) for Packaged Retail and Insurance-based Investment Products (PRIIPs). This is the standardised document made available to retail investors and containing key features of investment products, including how they might gain if they invest, the risks they are taking, and all the costs they will have to incur – with the ultimate aim of improving transparency in the investment market. PRIIPs are, for example, funds, structured securities, structured deposits and unit-linked and with-profits life insurance contracts.

Several issues arose with the first iteration of the RTS, including on performance scenarios (leading to overly pessimistic or optimistic results) and the transaction cost methodology (giving sometimes negative figures). These issues were largely anticipated by stakeholders and raised with regulators but were ultimately not fixed in the first version of the RTS. The review clause (originally set for 31 December 2018 but delayed by one year) is the opportunity for the ESAs to address these specific issues.

For the purpose of this consultation AMIC has decided to focus on and argue in favour of a review of the transaction cost methodology (currently the slippage methodology), given the confusion created by contradictory provisions across the EU (MiFID, Insurance Distribution Directive, PRIIPs and national provisions) and the potential knock-on effect on future EU rules. AMIC will call for replacement of the slippage methodology with the spread methodology for all asset classes. This approach also refers to indirect costs but removes many of the statistical impediments under the slippage methodology and the risk of disclosing misleading negative transactions costs. The spread methodology has the advantage that it is more suitable for *ex-ante* cost disclosures (and therefore the PRIIPs KID) that provide information about prospective investments. Most of the implicit costs (market impact, delay cost, opportunity cost) can already be integrated in the bid-ask spread.

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AMIC Sustainable Finance Working Group

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AMIC launched its Sustainable Finance Working Group in December 2019. Patrick Simion (BNPP AM) and Carey Evans (BlackRock) were appointed as Co-Chairs. The AMIC Sustainable Finance Working Group will provide a dedicated platform for buy-side members to: (i) issue positions on upcoming initiatives relevant to buy-side, in particular the review of the Non-Financial Reporting Directive, the disclosure regulation (RTS), the EU Ecolabel, and integration of sustainability risks and factors in the UCITS and AIFMD; (ii) identify concerns/priorities to be conveyed to the ICMA's Sustainable Finance Coordination Committee, managed by Nicholas Pfaff, which provides a forum for discussing sustainable finance in its entirety and brings together representatives from key ICMA Committees including AMIC; and (iii) exchange views on applicable market developments and innovations.

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Other buy-side regulatory developments

On 15 October 2019, EIOPA launched a public consultation, for comment by 15 January, on an Opinion that sets out technical advice for the 2020 review of Solvency II. This Opinion will respond to the call for advice of the European Commission of 11 February 2019 on the 2020 review of Solvency II, which comprises 19 separate topics – broadly covering: (i) review of the long term guarantee measures; (ii) potential introduction of new regulatory tools in Solvency II; and (iii) revisions to the existing Solvency II framework. In EIOPA's view, the Solvency II framework is overall working well, so the approach is in general one of evolution rather than revolution. In 2020 EIOPA will collect data in order to assess the quantitative combined impact of the proposals to be included in the advice. Considering all inputs, EIOPA will issue the finalised Opinion in June 2020.

On 2 December, EIOPA launched a public consultation, for comment by 2 March, on its approach to the RTS, ITS, and technical advice to the European Commission on delegated acts, as mandated by the PEPP Regulation. The consultation sets out EIOPA's current stances to approach the regulation of key aspects of the PEPP, underpinning the idea of establishing a simple, safe and cost-efficient savings product. EIOPA has already sought input from the supervisory community of the insurance and pension sectors, the other ESAs, and conducted an active dialogue with EIOPA's stakeholder groups and the Expert Practitioner Panel on PEPP. The key consultation considerations concern PEPP information documents; cost cap of the Basic PEPP; risk-mitigation techniques; supervisory reporting and cooperation between NCAs and EIOPA; and EIOPA's product intervention powers.

On 4 December, ESMA updated its Q&As on the application of AIFMD, adding one new Q&A on the AIFMD reporting to NCAs. Specifically, this new Q&A provides clarification on reporting requirements on liquidity stress tests for closed-ended unleveraged AIFs. The purpose of this Q&A document is to promote common supervisory approaches and practices in the application of the AIFMD and its implementing measures.

On 9 December, Regulation (EU) 2019/2088, of 27 November 2019, on sustainability-related disclosures in the financial services sector, was published in the EU's *Official Journal*. This Delegated Regulation entered into force on the 20th day following that of this publication, but generally it only applies from 10 March 2021 – with some specific provisions applying from 29 December 2019 and a few, regarding transparency of the promotion of environmental or social characteristics and of sustainable investments in periodic reports, not applying until 1 January 2022.

Also on 9 December, Regulation (EU) 2019/2089, of 27 November 2019, amending the EU BMR, as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks, was published in the EU's *Official Journal*. This Delegated Regulation entered into force on the day after this publication. Subsequently, on 20 December, the TEG published a *Handbook on Climate Benchmarks* and benchmarks' ESG disclosures. This follows on the publication of the *TEG Final Report on Climate Benchmarks*, published on 30 September. The aim of the handbook is to clarify those recommendations put forward by the TEG and to respond to FAQs from the market.

“ The Bank of England recommends measuring the liquidity of funds' assets using either a time liquidation methodology or price discount needed for a quick sell.

On 10 December, ESMA published the final report on the draft RTS under Article 25 of the ELTIF Regulation. Considering that the draft RTS depend to a large extent on the cost section of the PRIIPs KID, which is currently being revised in the context of the review of the delegated acts of PRIIPs, ESMA is of the view that it is preferable to postpone the finalisation of the draft RTS until the new PRIIPs delegated acts have been published. Therefore, this report provides a feedback statement summarising the responses received to the consultation on the draft RTS which was carried out between March and June 2019. Upon finalisation of the review of the PRIIPs Delegated Regulation, ESMA will assess the most appropriate way to finalise the draft ELTIF RTS.

On 12 December, ESMA issued its second annual report on sanctions (penalties and measures) imposed by NCAs under the UCITS Directive, covering the year 2018. While the number of NCAs issuing sanctions remains stable at 15, compared to the previous report for the period 2016-2017, the total number of sanctions issued has decreased based on a year on year comparison.

In its latest semi-annual *Financial Stability Report*, published on 16 December, the Bank of England takes stock of the ongoing review of fund liquidity provisions for open-ended funds conducted together with the FCA. This review is to be concluded in 2020, but the report already reveals interesting details. The Bank of England recommends measuring the liquidity of funds' assets using either a time liquidation methodology or price discount needed for a quick sell. Beyond this potential measurement requirement, we understand that the Bank of England is considering mandatory price adjustments for redeeming investors responsible for price discounts (eg swing pricing) and longer redemption notice period for funds according to the liquidity of underlying assets. Yet the Bank of England recognised that there are challenges to implementing these measures and it remains to be seen if and how this will be translated into the FCA's standards for open-ended funds.

On 18 December, ESMA published its findings on potential undue short-term pressures in securities markets. In its report, it makes recommendations to the Commission for action in key areas, such as:

- disclosure of Environmental, Social and Governance (ESG) factors including: amending the Non-Financial Reporting Directive (NFRD); promoting a single set of international ESG disclosure standards; and requiring the inclusion of non-financial statements in annual financial reports; and
- institutional investor engagement including: a review of the White List under the Takeover Bids Directive; a potential shareholder vote on the non-financial statement; and monitoring the application of the Shareholder Rights Directive.

The European Commission had asked the three ESAs to investigate potential sources of undue short-termism on corporations and provide advice on areas which regulators should address. Published in parallel, the EBA's report calls on banks to consider long-term horizons in their strategies and business activities. EIOPA reports that it found no clear evidence of undue short-termism in insurance and institutions for occupational retirement provision, although their investment practices are sensitive to macroeconomic circumstances such as the persistent low interest rate environment.

Separately, also on 18 December, the new EU covered bond legislation, comprising a Regulation and a Directive, has been published in the EU's *Official Journal*. The Regulation enters into force on the 20th day following this publication, but only applies as from 8 July 2022. The Directive also enters into force on the 20th day following this publication; however, the 18-month national transposition period will run to 8 July 2021, with national measures to be applied at latest by 8 July 2022 – alongside the Regulation.

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Buy-side oriented research

From 30 September to 6 October 2019, securities regulators, stock exchanges, international organizations, investor associations and other IOSCO stakeholders from some 90 jurisdictions participated in the third annual World Investor Week (WIW), a campaign to foster financial literacy and investor education and protection. The topics for this year´s WIW ranged from the basics of smart investing to online investments, digital assets and initial coin offerings.

On 25 October, EIOPA published its updated Risk Dashboard based on the second quarter 2019 Solvency II data, showing that the risk exposures of the European insurance sector remained overall stable compared to July. Macro and market risks continue at a high level and various factors are adding further pressure to the sector. Volatility of the largest asset class – bonds – increased, while credit risks continue at a medium level – with somewhat lower CDS spreads for most bond segments and broadly stable credit quality of asset portfolios. Nonetheless, signs of potential risk mispricing prevail. Profitability and solvency risks are also at a medium level. Market perceptions were marked by an underperformance of insurers' stocks compared to overall equity markets, whereas no change was observed in insurers' external ratings.

Published on 29 October, *Is Leverage Driving Procyclical Investor Flows? Assessing Investor Behaviour in UCITS Bond Funds* is an article in the ECB's latest semi-annual *Macroprudential Bulletin*. The authors report about the fact that a recent ECB study shows that leverage is an important driver in investors' redemption decisions. Regulatory changes to the UCITS framework facilitated the use of derivatives, increasing leverage for some European mutual funds which amplified investors' responsiveness to negative returns in a procyclical manner. They conclude that while the UCITS framework has contributed to the growth of the investment fund sector, possible regulatory shortcomings regarding the use of leverage may need to be further addressed.

Published on 31 October, *Investment Funds Under Stress* is an ECB staff working paper, in which the authors present a model for stress testing investment funds, based on a broad worldwide sample of primary open-end equity and bond funds. First, they employ a Bayesian technique to project the impact of macro-financial scenarios on country-level portfolio flows world-wide that are constructed from fund-level asset holdings. Second, from these projected country level flows, they model the scenarios' repercussions on individual funds along a three-year horizon. Importantly, they further decompose portfolio flows, disentangling the specific contributions of transactions, valuation and foreign exchange effects.

Overall, the authors' results indicate that the impact of a global adverse macro-financial scenario leads to a median depletion in AUM of 24% and 5%, for euro area-domiciled equity and bond funds respectively, largely driven by valuation effects. Scenario and results both present similarities to the global financial crisis. They use historical information on fund liquidations to estimate a threshold for a drop in AUM that signals a high likelihood of a forthcoming liquidation. Based on this, they estimate that 5.8% and 0.5% of euro area-domiciled equity and bond funds respectively could go into liquidation. Such empirical thresholds can be useful for the implementation of prudential policy tools, such as redemption gates.

Published on 6 November, *Swing Pricing and Fragility in Open-end Mutual Funds* is an IMF staff working paper, in which the authors consider the question: how to prevent runs on open-end mutual funds? In recent years, markets have observed an innovation that changed the way open-end funds are priced. Alternative pricing rules, known as swing pricing, adjust funds' net asset values to pass on funds' trading costs to transacting shareholders. Using unique data on investor transactions in UK corporate bond funds, the authors show that swing pricing eliminates the first-mover advantage arising from the traditional pricing rule and significantly reduces redemptions during stress periods. The positive impact of alternative pricing rules on fund flows reverses in calm periods when costs associated with higher tracking error dominate the pricing effect.

Published on 6 November, *Turning up the Heat – Climate Risk Assessment in the Insurance Sector* is an insight paper from the Financial Stability Institute. The authors note that climate risks are recognised as a critical threat to society, with potentially adverse implications for financial stability and the viability of insurers. Efforts have been made by insurance supervisors and insurers in some jurisdictions to better understand climate risks, but further efforts are needed. To facilitate a better understanding in this area, this paper examines the different regulatory approaches currently in place relating to climate risk assessment, in particular through enterprise risk management frameworks.

The paper also describes how some supervisory authorities have undertaken climate risk assessment exercises, focusing on stress test and scenario analysis approaches. In general, the paper finds that risk quantification techniques and models that consider climate risks are more advanced for physical risks but are still at an early stage for transition and liability risks. Looking ahead, there is room to enhance international cooperation among insurance supervisors, and within financial policy and regulatory forums to improve understanding of climate risks and their potential impact on firms, policyholders and financial stability. Other key policy issues that require consideration include the impacts of climate risks on access and affordability of insurance products, and the potential use of capital requirements to address climate risks.

On 14 November, the FSB welcomed the finalisation and publication of the IAIS *Holistic Framework for Systemic Risk in the Insurance Sector*, for implementation in 2020. The key elements of the framework are: an enhanced set of supervisory policy measures for macroprudential purposes; a global monitoring exercise by the IAIS designed to assess global insurance market trends and developments and detect the possible build-up of systemic risk in the global insurance sector; mechanisms to allow for a collective assessment of potential global systemic risk and a coordinated supervisory response when needed; and an assessment by the IAIS of the consistent implementation of the enhanced supervisory policy measures and powers of intervention.

In light of the finalised holistic framework, the FSB, in consultation with the IAIS and national authorities, has decided to suspend the identification of Global Systemically Important Insurers (G-SII), as from the beginning of 2020. In November 2022, the FSB will, based on the initial years of implementation of the holistic framework, review the need to either discontinue or re-establish an annual identification of G-SIIs by the FSB in consultation with the IAIS and national authorities. The FSB will receive from the IAIS an annual update of the outcomes of the global monitoring exercise, including the IAIS assessment of systemic risk in the global insurance sector and the supervisory response to identified risks (if any).

On 16 December, EIOPA published a report on insurers' asset and liability management in relation to the illiquidity of their liabilities. This supplements information provided in EIOPA's annual reports on long-term guarantee measures and is published in response to a request from the European Commission in the context of the 2020 Review of Solvency II. The report provides information on: insurance liabilities; the asset management of insurers; long-term guarantee measures, including matching adjustment, volatility adjustment, actual yield and dynamic volatility adjustment; and the market valuation of insurance liabilities. EIOPA will draw upon the analysis in this report in its Opinion on the 2020 Review of Solvency II.

Published on 16 December, *Shadow Banking and Financial Stability Under Limited Deposit Insurance* is an ESRB working paper. The author studies the case where shadow banks issue only uninsured deposits while commercial banks issue both insured and uninsured deposits. The effect of shadow banking on financial stability is ambiguous and depends on the (exogenous) upper limit on insured deposits – if the upper limit on insured deposits is high, then the presence of a shadow banking sector is detrimental to financial stability; and, by contrast, if the upper limit on insured deposits is low, then the presence of a shadow

While runs may occur in the shadow banking sector, the situation without shadow banks, and hence with a larger amount of uninsured deposits held at commercial banks, is worse.

banking sector is beneficial to financial stability. While runs may occur in the shadow banking sector, the situation without shadow banks, and hence with a larger amount of uninsured deposits held at commercial banks, is worse.

On 17 December, EIOPA published the results of its 2019 *Institutions for Occupational Retirement Provisions (IORPs) Stress Test*. This found that the adverse scenario would wipe off almost one quarter of the investment assets' values in the sample, totalling €270 billion, with market risks leading to substantial benefit reductions and increase of sponsor support. Extended cash flow analysis shows timing of expected impact is high in the first years on sponsors, while the effects of benefit reductions would drag on for decades should the short-term effects become permanent. The first European analytical element on sustainability risks sheds light on the current management and consideration of ESG factors in the IORP sector, indicating a high carbon footprint, relative to EU economy, in the sample's equity investments. The majority of IORPs indicate consideration of ESG factors, yet less than 20% of those in the sample currently assess the impact of ESG factors on risks and return.

On 18 December, EIOPA published its *December 2019 Financial Stability Report* of the (re)insurance and occupational pensions sectors in the EEA. It finds that the risk of a prolonged low yield environment has intensified over the last six months and remains the key challenge for European insurers and pension funds, putting pressure on both solvency positions and long-term profitability. The combination of weakening economic outlook, concerns over debt sustainability and stretched valuations across financial markets could also give rise to a sudden reassessment of risk premia. Emerging cyber and climate change related risks, along with interconnectedness with banks and home-bias in investments are also all matters of high concern.

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AMIC Conference

The latest AMIC Conference took place on 27 November 2019 in London, hosted by BlackRock. The AMIC holds two plenary conference sessions annually to help advise the Executive Committee of AMIC on priorities and to discuss current issues. These meetings also provide excellent networking opportunities for the AMIC community.

The event started with a keynote speech from Fabrice Demarigny, who outlined the report of the Next Capital Markets Union (CMU) High-Level Expert Group which he chaired, with particular consideration of the implications of this for the buy side of the market.

Following on the CMU theme, there was a panel on STS securitisation where industry experts did a stocktaking exercise of all the developments in the securitisation market from an investor, issuer and third-party verifier perspectives and then moved on to discuss whether the STS Regulation is meeting the objectives set by CMU.

Andy Hill, ICMA Senior Director, presented initial findings of the third ICMA study report on the European corporate bond secondary market and the results of *ICMA's Assessment of the Impacts of the EU CSDR Mandatory Buy-in Regime on the European Bond Markets*.

AMIC Chairman Robert Parker gave an overview of indicators of investment sentiment, including: the most crowded trades, tail risks, sector and asset allocation and overvalued markets. He also reviewed the performance in the first half of 2019 of asset classes and economic indicators, including monetary conditions, GDP forecasts, inflation trends, business and consumer confidence and economic surprises.

The next item was a panel on addressing the pension funding gap where industry experts debated the forthcoming Pan European Pension Plan (PEPP) product, whether it will be widely used and thus help address the gap. The panel then discussed the current negative rate environment and the challenges it is for asset managers and pension funds to meet their obligations while staying invested in low risk assets.

The last panel of the day was a pragmatic take on sustainable finance, considering what the sustainable finance trend means for investment managers' strategies and funds, and whether there is a need for a potential EU-wide Ecolabel for funds.

The latest AMIC Review was published on the day of the event with a focus on current policy developments and market trends, including fund liquidity, the impact of negative yields on asset management and the case for a consolidated tape for cash bonds.

The next AMIC conference will take place in Paris on 11 March 2020.

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International Regulatory Digest

 

by David Hiscock and Alexander Westphal

G20 financial reform developments

On 2 October 2019, the BCBS published the results of its latest Basel III monitoring exercise, based on data as of 31 December 2018. The report sets out the impact of the Basel III framework that was initially agreed in 2010 as well as the effects of the BCBS's December 2017 finalisation of the Basel III reforms, and, for the first time, it also reflects the finalisation of the market risk framework published in January 2019. Data are provided for a total of 181 banks, including 105 large internationally active banks. The final Basel III minimum requirements are expected to be implemented by 1 January 2022 and fully phased in by 1 January 2027.

Additionally, on 2 October, the Board of IOSCO published two update reports entitled *Update to the IOSCO Peer Review of Regulation of Money Market Funds* and *Update to the IOSCO Peer Review of Implementation of Incentive Alignment Recommendations for Securitisation*. The MMF report finds that most jurisdictions have implemented the fair value approach for the valuation of MMF portfolios, but progress in liquidity management is less advanced and less even. The securitisation report finds that, overall, progress remains mixed across participating jurisdictions in implementing the IOSCO recommendations for incentive alignment for securitisation.

On 11 October, the FSB and IMF published the *Fourth Progress Report – Countdown to 2021*, on the implementation of the Second Phase of the G20 Data Gaps Initiative (DGI-2). The report was submitted to the G20 Finance Ministers and Central Bank Governors ahead of their meetings in Washington D.C. in mid-October. This report provides an overview of the progress since September 2018 and the challenges that remain in implementing the DGI-2 recommendations until the final deadline of 2021. The report highlights that participating economies made additional progress in closing the identified data gaps and promoting the regular flow of timely and reliable statistics for policy use, but challenges remain in fully implementing the DGI-2 recommendations by 2021.

On 13 October, the FSB published a letter from its Chair, Randal K. Quarles, to G20 Finance Ministers and Central Bank Governors, ahead of their meetings in Washington D.C. The letter notes that the development of post-crisis reform policies is nearly complete, and implementation is well underway. Yet it emphasises that the FSB's mission is far from complete. Implementation progress on agreed G20 reforms remains uneven across key reform areas, and the FSB is in the process of evaluating that reforms are working as intended.

Looking ahead, authorities need to be ready to address evolving risks to global financial stability, be they related to current downside risks to growth and uncertainties around Brexit, or structural changes in the financial system. The letter highlights three areas of the FSB's ongoing work: (i) ensuring resilience in the face of new risks; (ii) potential financial stability issues from global stablecoins; and (iii) promoting a financial system that supports strong and sustainable global growth.

On 14 October, the FSB published an update on its work on market fragmentation, which has also been delivered to the G20 Finance Ministers and Central Bank Governors for their meeting. The update provides information on current plans and steps already taken, to implement work in the four areas identified by the FSB in its June report on market fragmentation, namely: (i) deference; (ii) pre-positioning of capital and liquidity; (iii) regulatory and supervisory coordination and information-sharing; and (iv) market fragmentation as part of the evaluation of reforms, starting with the FSB's ongoing too-big-to-fail evaluation.

On 16 October, the FSB published its 2019 annual report on the implementation and effects of the G20 financial regulatory reforms, which was delivered to the G20 meeting and sets out that implementation of the reforms called for by the G20 after the global financial crisis is progressing. This is contributing to an open and resilient financial system that supports the efficient provision of financing to the real economy. Yet it is critical to maintain momentum and avoid complacency, in order to fully achieve the goal of greater resilience as vulnerabilities are evolving. Rapid structural and technological change requires continued vigilance to maintain a sound and efficient financial system. An open and resilient financial system, grounded in agreed international standards, is crucial to support sustainable growth and requires the support of the G20 in implementing the agreed reforms and reinforcing global regulatory cooperation.

Also on 16 October, the BCBS issued the 17th progress report on adoption of the Basel regulatory framework, which sets out the adoption status of Basel III standards for each Committee member jurisdiction as of end-September 2019. It includes the Basel III post-crisis reforms published by the BCBS in December 2017 and the finalised minimum capital requirements for market risk in January 2019, which will take effect from 1 January 2022. Since the previous report, published in May 2019, member jurisdictions have made further progress in adopting Basel III standards, notably the standard on interest rate risk in the banking book, the NSFR and the supervisory framework for measuring and controlling large exposures. However, the report also shows that a number of jurisdictions have yet to put these standards into effect.

Published on 16 October, the latest edition of the IMF's semi-annual *Fiscal Monitor* emphasizes the environmental, fiscal, economic, and administrative case for using carbon taxes, or similar pricing schemes such as emission trading systems, to implement climate mitigation strategies. It provides a quantitative framework for understanding their effects and trade-offs with other instruments and applies it to the largest advanced and emerging economies. Alternative approaches, like "feebates" to impose fees on high polluters and give rebates to cleaner energy users, can play an important role when higher energy prices are difficult politically. At the international level, the report calls for a carbon price floor arrangement among large emitters, designed flexibly to accommodate equity considerations and constraints on national policies. The report estimates the consequences of carbon pricing and redistribution of its revenues for inequality across households. Strategies for enhancing the political acceptability of carbon pricing are discussed, along with supporting measures to promote clean technology investments.

On 17-18 October, G20 Finance Ministers and Central Bank Governors met, in Washington. Following from this meeting, press releases were issued regarding international taxation and global stablecoins, together with reports, by the FSB and the FATF, relating to the latter. Also related to this, a CPMI paper, *Investigating the Impact of Global Stablecoins*, was published, on 18 October, which lays out initial recommendations for both private sector stablecoin developers and public sector authorities to address the challenges and risks of stablecoins.

On 19 October, a communiqué was issued following the 40th meeting of the IMFC, which was held in Washington alongside the Annual Meetings of the Boards of Governors of the World Bank Group and the IMF. Statements given on the occasion of the IMFC meeting and related documents are available. Among other things, in the segment on *Global Outlook and Policy Priorities*, the IMFC communiqué states that:

- We will continue to monitor and, as necessary, tackle financial vulnerabilities and risks to financial stability, including with macroprudential policies.
- We will enhance our efforts to reduce policy uncertainty and strengthen international frameworks and cooperation.

Rapid structural and technological change requires continued vigilance to maintain a sound and efficient financial system.

- We stress the importance of timely, full, and consistent implementation and finalization of the financial sector reform agenda as soon as possible, and the ongoing evaluation of the effects of these reforms.
- We will also address fragmentation through continued regulatory and supervisory cooperation, adapt financial regulation to structural changes and the evolving global financial landscape, and close data gaps.
- We will continue to work together to enhance debt transparency and sustainable financing practices by both debtors and creditors, public and private; and strengthen creditor coordination in debt restructuring situations, drawing on existing fora.
- We support efforts toward achieving the 2030 Sustainable Development Goals.
- We will continue to support domestic and multilateral efforts to address, build resilience to, and deal with the macroeconomic consequences of pandemics, cyber risks, climate change and natural disasters, energy scarcity, conflicts, migration, and refugee and other humanitarian crises.
- We will continue to collaborate to leverage financial technology while addressing related challenges.

The BCBS met, on 30-31 October, to discuss a range of policy and supervisory issues, and to take stock of its members' implementation of post-crisis reforms. Among other things, the BCBS:

- agreed to consult on a set of revised disclosure requirements related to the market risk framework finalised in January 2019, and to consult on disclosure templates related to banks' sovereign exposures which would be voluntary in nature, with jurisdictions free to decide whether or not to implement them;
- agreed to publish a discussion paper on the prudential treatment of crypto-assets and a report on open banking and APIs; and, going forward, to conduct a set of "deep dive" assessments related to certain specified aspects of FinTech;
- took stock of benchmark rate reforms, and discussed the potential regulatory and supervisory implications stemming from banks' transition to alternative reference rates; and will consider whether any further regulatory or supervisory measures are warranted to help achieve this outcome; and
- exchanged views on work on climate-related financial risks.

On 31 October, the BCBS published a newsletter to reiterate the importance of the capital buffer framework – which comprises the capital conservation buffer, and by extension the countercyclical capital buffer and buffers for systemically-important banks – and to emphasise that buffers, which are an important feature of the Basel III framework complementary to its minimum capital requirements, are designed to be usable. While each of these buffers seeks to mitigate specific risks, they share similar design features. Albeit that using capital buffers will assist banks in absorbing losses while continuing to provide key services to the real economy, the BCBS is of the view that banks should always seek to rebuild their capital strength in a timely manner.

On 7 November, the FSB Plenary met in Paris. Considering current vulnerabilities in the global financial system, the Plenary discussed the financial stability implications of structural changes in the interest rate environment that have been occurring over a number of years and discussed a report assessing vulnerabilities associated with leveraged loans and CLOs, which was subsequently published, on 19 December.

It was noted that the resilience of the financial system has improved as a result of regulatory reforms and that most financial markets have continued to operate well despite recent episodes of short-lived stress, but that a future more widespread deterioration in market liquidity, or increase in volatility, could test market resilience. Given rising global vulnerabilities, authorities should continue to assess whether existing buffers are adequate to support resilience, taking into account their domestic conditions and cyclical position. FSB members also reviewed progress on the development of a new surveillance framework, which will support the comprehensive, methodical and disciplined review of vulnerabilities by the FSB, and thereby help to identify and address new and emerging risks to financial stability.

The Plenary discussed developments in crypto-asset markets, with members endorsing an augmented framework for monitoring potential financial stability risks in those markets to take account of the development of so-called global stablecoin systems, recognising that these are developing rapidly. The FSB will publish a consultative report on regulatory issues of stablecoins in April 2020. FSB members also discussed the FSB's ongoing work on market developments and potential financial stability implications from the entry of BigTech firms into finance and from third-party dependencies in cloud services, with initial reports on these key topics to be published in the coming weeks.

FSB members took stock of progress with the FSB's ongoing evaluation of too-big-to-fail reforms for systemically important banks, on which the FSB will publish a consultation report in June 2020 and complete the work by end-2020. The FSB's evaluation of the effects of financial regulatory reforms on the financing of SMEs was nearing completion, with the final report subsequently published, on 29 November. FSB members agreed that the next evaluation will be on the effects of MMF reforms, as the first of a number of future evaluations on non-bank financial intermediation. FSB members also discussed the FSB's work programme for 2020, which was subsequently published, on 17 December, including deliverables to Saudi Arabia's 2020 Presidency of the G20. The Plenary agreed to a set of recommendations for enhancing the effectiveness of the FSB's Regional Consultative Groups and also agreed to streamline the FSB's working group structure.

On 14 November, following on from its meeting in Madrid on 30-31 October, the BCBS published two consultative documents related to Pillar 3 disclosure (each for comment by 14 February). The first document proposes a set of revised disclosure requirements related to the market risk framework finalised in January 2019; and the second consults on voluntary disclosure templates related to banks' sovereign exposures.

Also on 14 November, the FSB published its 2019 Resolution Report, which provides an update on progress in implementing policy measures to enhance the resolvability of SIFIs and sets out plans for further work. The report concludes that authorities and firms need to be mindful of any remaining gaps as they work towards making resolution strategies and plans operational in all sectors, ie CCPs, banks and insurance. The FSB also welcomed the finalisation and publication of the IAIS *Holistic Framework for Systemic Risk in the Insurance Sector*, for implementation in 2020.

On 22 November, the FSB published the 2019 list of G-SIBs, using end-2018 data and an assessment methodology designed by the BCBS. One bank, Toronto Dominion, has been added to the list of G-SIBs that were identified in 2018, and therefore the overall number of G-SIBs increases from 29 to 30. Alongside this, the BCBS published updated denominators used to calculate banks' scores and the values of the underlying twelve indicators for each bank in the assessment sample. The BCBS also published the thresholds used to allocate the G-SIBs to buckets, as well as updated links to public disclosures of all banks in the sample.

On 26 November, a statement on proportionality was published jointly by the BCBS and the Basel Consultative Group (BCG). The BCBS expects the Basel Framework – encompassing the Basel III standards – to be implemented in full by BCBS member jurisdictions, for internationally active banks. Nevertheless, the BCBS and the BCG support the use of proportionality in implementing the framework in a manner consistent with the core principles for effective banking supervision – noting that the framework envisions a range of approaches, from simpler standardised approaches to advanced approaches. A proportionate regulatory framework should not reduce the resilience of banks or dilute the prudential regulatory framework, but rather reflect the relative differences in risk and complexity across banks and the markets in which they operate; and should also consider supervisory capacity and resources, particularly when implementing more complex standards.

The Kingdom of Saudi Arabia assumed the 2020 G20 Presidency, on 1 December. The Kingdom will guide the work of the G20 under the theme of *Realizing Opportunities of the 21st Century for All* and will focus on three aims: (i) empowering people; (ii) safeguarding the planet; and (iii) shaping new frontiers. Under (iii), it is interesting to note that the Presidency's agenda, besides work on enabling the digital economy, includes addressing the entry of BigTech in finance, stating that: "A concerted effort is needed from the G20 to tackle all aspects of the phenomenon, including financial stability, implications on the conduct of monetary policy and the functioning of government debt markets, ensuring a level-playing-field with financial institutions and data protection issues, as well as the potential impact of private currencies' issuance at a large scale."

The first official event for the Saudi G20 Finance Track was held, on 5 December, with a symposium in the Kingdom's capital, Riyadh. Subsequently, on 6-7 December, G20 Finance and Central Bank Deputies met, in Riyadh. They will meet again, in February, in Riyadh to resume discussions on the Finance Track

The BCBS and the BCG support the use of proportionality in implementing the framework in a manner consistent with the core principles for effective banking supervision

work programme ahead of the 1st G20 Finance Ministers' and Central Bank Governors' meeting, to be held in Riyadh on 22-23 February. Riyadh will welcome G20 leaders to the 2020 Leaders' Summit, as the culmination of the Saudi G20 Presidency, on 21-22 November.

On 16 December, IOSCO requested feedback, by 16 February, on proposed guidance to help IOSCO members address potential conflicts of interest and associated conduct risks arising from the role of market intermediaries in the debt capital raising process. IOSCO notes that conflicts of interest and associated conduct risks can weaken investor confidence and undermine debt capital markets as an effective vehicle for issuers to raise funding. This consultation is intended to help regulators identify and address these risks; and, among other things, seeks public comments on the use of DLT in bond issuances and the potential benefits and risks of using this technology, including for managing conflicts of interest.

Also on 16 December, the BCBS launched its consolidated Basel Framework, which brings together all of its global standards for the regulation and supervision of banks and presents them on a new section of its website. In April 2019, the BCBS issued a draft version of the consolidated Basel Framework, which focused on reorganising existing requirements and not introducing new requirements or otherwise amending the standards previously agreed.

The preparation of the standards in the new framework format did, however, reveal some inconsistencies between Basel requirements as well as ambiguities that needed to be addressed through minor policy changes, which the BCBS concurrently consulted upon. Considering the feedback this new publication sets out the changes that the Committee agreed to make relative to that earlier draft version of the framework and lists the new FAQs added to the framework since its publication in draft form, in April 2019.

On 17 December, the FSB published its work programme for 2020, with its 2020 work priorities reflecting the evolving nature of the global financial system and associated risks to financial stability. The FSB will reinforce its forward-looking monitoring of developments to identify, assess and address new and emerging vulnerabilities. At the same time, the FSB will continue its work to finalise and operationalise the remaining elements of post-crisis reforms; monitor and assess the implementation of reforms; and evaluate their effects in order to ensure that reforms work as intended. Important specific FSB work programme items, which include key deliverables to the G20 Saudi Arabian Presidency, are in respect of FinTech; global stablecoins; cross-border payment systems; interest rate benchmarks; and ongoing evaluation work.

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European financial reform developments

CMU

On 2 October 2019, the EBA published two reports, which monitor the impact of implementing the final Basel III reforms and the current implementation of liquidity measures in the EU. The EBA Basel III capital monitoring report presents an assessment of the impact of the full implementation (to 2027) of the Basel III package on EU banks, based on data as of 30 June 2018. Overall, the EBA estimates that the Basel III reforms, once fully implemented, would determine an average increase by 19.3% of EU banks' Tier 1 minimum required capital. The LCR, which was fully implemented in January 2018, stood at around 149% on average in June 2018, well above the minimum threshold of 100%.

Also on 2 October, the Joint Committee of the three ESAs published its *2020 Work Programme*. In 2020, under the EBA's chairmanship, the Joint Committee will continue its work in the areas of cross-sectoral risk analysis, consumer protection, financial conglomerates, securitisation as well as accounting and auditing. Areas of particular focus of its work will be on PRIIPs, financial innovation – also in relation to the European Commission's FinTech Action Plan and the work of the European Forum for Innovation Facilitators (EFIF) – as well as sustainable finance and securitisation.

On 8 October, the European Parliament's ECON and EMPL Committees held a hearing for Valdis Dombrovskis, Executive Vice-President and Commissioner-designate for An Economy that Works for People. In his written answers to the European Parliament questionnaire Commissioner-designate Dombrovskis states, among other things, that "We have to continue our work on building a strong EMU to help Europe project its full economic weight in the world. We need to give the euro a greater international role. This means completing the Banking Union by finding a way forward on its missing pillar – the EDIS. In parallel, we should strengthen our work to fight against money laundering: there is no place for dirty money in European banks. I regard the CMU as high priority because it is instrumental for facilitating access to finance for our SMEs, which are the backbone of our economy and job creation."

"While Europe is home to immense talent and innovation, our SMEs find it difficult to become largescale innovators, often due to insufficient access to finance." Also, "The transition to climate neutral economy will require massive investment, both from public and private sources." To bridge the gap and building on my experience with sustainable finance policy, I would work to develop a new Sustainable Finance Investment Plan." And, furthermore, "We should also harness the potential of new digital technologies to deliver a better deal for European consumers, while protecting the integrity and stability of the European financial system. To that effect, I commit to continue work on FinTech and to propose a common EU approach on cryptocurrencies." The Parliament has published a summary of his commitments.

Savings and Sustainable Investment Union, the report of the Next CMU High-Level Group, as delivered to Ministers and presented to the Finnish Presidency, was published on 9 October. The task put by the Ministers to the Next CMU Group was to analyse, with a "fresh eye", the EU's market-based financing capacity five years after the launch of the CMU and to make appropriate recommendations. The Next CMU Group proposes that the CMU should be renamed as the "Savings and Sustainable Investment Union" and invites political leaders to focus on two EU major objectives: (i) adopting and promoting a capital market that offers saving products to serve citizens' needs and that allocates capital to value creating investments in the real, innovating and sustainable economy; and (ii) building/strengthening an integrated, competitive, deep and liquid European capital market, to maintain the EU as one of the top two financial centres of the world.

To do so, the Next CMU Group has reached the conclusion that strong and determined political action on an EU and national level should focus on four capital market components, where significant progress can be achieved and drive the entire process to create a deeper and more robust capital market for the EU. The report is articulated around each absolute priority, for which the Next CMU Group proposes specific recommendations with real transformational effect. In addition, it has identified several areas where key objectives and indicators could be developed to periodically measure progress.

The Next CMU Group has reached the conclusion that strong and determined political action on an EU and national level should focus on four capital market components, where significant progress can be achieved

During the ECOFIN Council meeting, on 10 October, the Chair of the Wise Persons' Group on the European financial architecture for development presented the final report – *Europe in the World: The Future of the European Financial Architecture for Development* – on how to maximise the added value of the European financial architecture for development, taking into account existing national and international bodies involved. The report argues in support of consolidating and streamlining development finance and climate activities outside the EU into a single entity, a "European Climate and Sustainable Development Bank". Following discussion, the Finnish Presidency committed to deal with this issue as a matter of priority and Council conclusions on the report were subsequently adopted, on 5 December.

On 11 October, the Commission launched a public consultation on implementing the final Basel III reforms in the EU, for comment by 3 January. This consultation aims to gather views on specific topics in the areas of credit risk, operational risk, market risk, credit valuation adjustment risk and SFTs, as well as in relation to the output floor. Beyond these topics related to the Basel III implementation, views are also welcomed on certain other subjects with a view to ensuring convergent and consistent supervisory practices across the EU and alleviating the administrative burden.

The inaugural meeting of the Joint EU-Japan financial regulatory forum was held in Tokyo, on 11 October, providing an important opportunity for senior officials from both sides to exchange views on the recent regulatory and supervisory developments in the financial sector at international level and in their respective jurisdictions. The participants: (i) discussed the regulatory cooperation framework under the Japan-EU EPA, as well as the EU's equivalence and the Japanese deference frameworks; (ii) used the opportunity to brief each other on the recent developments in the financial sector in the EU and in Japan, mainly in the banking sector and capital markets; (iii) discussed their respective initiatives in the field of sustainable finance; and (iv) exchanged letters on cooperation in the area of banking resolution. The next such forum meeting is foreseen to take place in Brussels, in 2020.

During its meeting on 17-18 October, the European Council adopted conclusions on, among other things, the MFF, the next institutional cycle and climate change. During the meeting, the European Council exchanged views with President-elect Ursula von der Leyen, on the Commission's contribution to the implementation of the EU's priorities, and formally confirmed the appointment of Christine Lagarde as President of the ECB, for a non-renewable term of eight years. Christine Lagarde replaced the outgoing President, Mario Draghi, as of 1 November 2019.

Following on from political agreements reached in Q1 2019, on 8 November, it was announced that the European Council has adopted a set of legislative reforms which are part of progress towards CMU. The texts, all of which were subsequently signed in Strasbourg, in the week of 25 November, ready for publication in the EU's *Official Journal*, concern: (i) the creation of a new category of benchmarks contributing to sustainable finance; (ii) transparency obligations for sustainable investments; (iii) a new prudential framework for investment firms; (iv) a harmonised framework for covered bonds; and (v) rules promoting access to SME growth markets. Remarks by Mário Centeno, following the Eurogroup meeting of 7 November, include some update on discussions regarding euro area reforms, including EDIS.

Following from an earlier call for members, on 18 November, the , the European Commission announced the composition of a new High-Level Forum (HLF) on CMU. This HLF will feed into the work on future CMU policies, proposing targeted policy recommendations for future CMU actions; and is being chaired by Thomas Wieser (former Chair of the European Financial Committee).

The work of this HLF has already commenced and is organised in three subgroups, focussing on the following areas: (i) building a pan-European ecosystem for raising capital for companies, including SMEs; (ii) fostering retail investor participation and diversification of the investor base; and (iii) strengthening a pan-European financial market architecture. The subgroups are each chaired by a sub-Chair: David Wright for the capital ecosystem one, Maria Luis Albuquerque for retail investor participation, and Peter Praet for financial market architecture. The work of the different sub-groups will flow together to culminate in an interim report, currently planned for February 2020, with the final report to be delivered to the Commission in May 2020.

On 21 November, the EBA published a set of roadmaps outlining its approach and timelines for delivering the mandates stemming from the *Risk Reduction Measures Package* adopted, on 20 May, by the Council of the EU and the European Parliament. These mandates are mainly focused in the areas of governance and remuneration, large exposures, resolution as well as reporting and disclosure. Besides clarifying the sequencing of mandates and the rationale behind their prioritisation, the roadmaps aim at providing a preliminary understanding of the mandates combined with some policy guidance.

On 1 December, the von der Leyen Commission took office. Ursula von der Leyen, President of the European Commission, attended a ceremony at the House of European History in Brussels on to mark the 10th anniversary of the Treaty of Lisbon and, on this occasion, received the Treaties from David Sassoli, President of the European Parliament, in a symbolic hand-over. Her brief remarks during the ceremony have been published and the Political Guidelines and priorities for her mandate are available.

The last ECOFIN meeting under the Finnish Presidency was held, on 5 December, in Brussels, preceded by a Eurogroup meeting, on 4 December. In his opening remarks at the subsequent ECOFIN press conference, Executive Vice-President Dombrovskis observed that this ECOFIN had a very green flavour to it, with many discussions related to tackling climate change and to finding best solutions to finance the transition to the climate neutral economy. He also highlighted discussions regarding tackling money laundering and terrorist financing, which are being taken seriously given a number of money laundering scandals across the EU. In addition, he reported that the ECOFIN endorsed a joint statement with the Commission on stablecoins, which are part of a much broader universe of crypto assets, and expressed his delight to see so much support for the CMU, which now needs to be taken to the next level.

The Council adopted conclusions setting out objectives for a further deepening of the CMU. These conclusions, which will shape the format and scope of a new roadmap for future action to further integrate the capital markets of EU Member States, set out six main objectives for deepening the CMU, namely: (i) enhanced access to finance for EU businesses, especially SMEs; (ii) removal of structural and legal barriers for increased cross border capital flows; (iii) provision of incentives and removal of obstacles for well-informed retail savers to invest; (iv) support for the transition to sustainable economies; (v) embracing technological progress and digitalization; and (iv) strengthened global competitiveness. The Commission is invited to come forward with a set of clearly defined, objective, targeted, effective and adequate KPIs, by the end of 2020; and to assess and explore the measures outlined in an annex to the conclusions, and to identify potential gaps for further measures as well as take into account measures already adopted, in its future work on the CMU.

Considering climate action, the Council adopted conclusions on the EU energy taxation framework, giving its support to an update of the legal framework for energy taxation which will contribute to wider economic and environmental policy objectives. The Council also approved a work plan on climate action, which will establish regular policy discussions on climate action at the ECOFIN Council, and discussed the future agenda for sustainable finance.

On 4 December, the EBA published the second part of its advice on the implementation of Basel III in the EU (complementing a report published on 5 August). This includes an assessment of the impact of the revisions to the credit valuation adjustment and market risk frameworks, and the corresponding policy recommendations. It also provides a macroeconomic impact assessment of the full Basel III package. When accounting for the 2019 FRTB standards, the impact assessment shows that the full implementation of Basel III, under conservative assumptions, will increase the current minimum capital requirement by 23.6% on average, and would imply an aggregate shortfall in total capital of €124.8 billion. The macroeconomic impact assessment shows that the implementation of Basel III will have net benefits for the EU economy.

On 11 December, the European Commission presented *The European Green Deal*, which provides a roadmap with actions to boost the efficient use of resources by moving to a clean, circular economy and stop climate change, reverse biodiversity loss and cut pollution. It outlines investments needed and financing tools available; and explains how to ensure a just and inclusive transition. *The European Green Deal* covers all sectors of the economy, notably transport, energy, agriculture, buildings, and industries such as steel, cement, ICT, textiles and chemicals.

Meeting the objectives of *The European Green Deal* will require significant investment. Achieving the current 2030 climate and energy targets is estimated to require €260 billion of additional annual investment, representing about 1.5% of 2018 GDP. This investment will need the mobilisation of the public and private sectors. The Commission will present in early 2020 a Sustainable Europe Investment Plan to help meet investment needs. At least 25% of the EU's long-term budget should be dedicated to climate action, and the EIB, Europe's climate bank, will provide further support. For the private sector to contribute to financing the green transition, the Commission will present a *Green Financing Strategy* in 2020.

Section 2.2.1 of the Commission's Communication elaborates on the fact that the private sector will be key to financing the green transition. Long-term signals are needed to direct financial and capital flows to green investment and to avoid stranded assets. The Commission will present a renewed sustainable finance strategy in the third quarter of 2020 that will focus on a number of actions. First, the strategy will strengthen the foundations for sustainable investment, requiring adoption of the taxonomy and further embedding sustainability into the corporate governance framework. At the same time, companies and financial institutions will need to increase their disclosure on climate and environmental data so that investors are fully informed about the sustainability of their investments – to this end, the Commission will review the Non-Financial Reporting Directive.

Second, increased opportunities will be provided for investors and companies by making it easier for them to identify sustainable investments and ensuring that they are credible – this could be done via clear labels for retail investment products and by developing an EU green bond standard. And, third, climate and environmental risks will be managed and integrated into the financial system – better integrating such risks into the EU prudential framework and assessing the suitability of the existing capital requirements for green assets.

From 1 January 2020, Croatia has assumed the Presidency of the EU, for the first half of 2020, following Finland and preceding Germany. As announced on 30 October, a Europe that develops, connects and protects and is influential on the global scene are the four pivotal areas of Croatia's Presidency. Alongside this, the Croatian Presidency published a document specifying its programme priorities.

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Macroprudential risk

Published on 1 October 2019, *Fragmentation in Global Financial Markets: Good or Bad for Financial Stability?* is a BIS staff working paper. The author observes that the many regulatory reforms following the great financial crisis of 2007-2009 have most often been designed and adopted through an international cooperative process. As such, actions have tended to harmonise national approaches and diminish inconsistencies. Nevertheless, some market participants and policy makers have recently raised concerns over an unwanted and unnecessary degree of fragmentation in financial markets globally, with possibly adverse effects for financial stability. This paper reviews the degree of fragmentation in various markets and classifies its possible causes. It then reviews whether fragmentation is necessarily detrimental to financial stability, suggesting that, as is more likely, various trade-offs exist. It concludes by outlining areas for further analysis.

On 2 October, the ESRB reported on the 35th regular meeting of its General Board, on 26 September, at which the Board discussed the rising threat of protectionism and the geopolitical uncertainties that have led to a further deterioration in the outlook for growth. Among other things, the Board noted that the provision of financial services across borders is an important feature of ongoing financial integration in the EU and, in this regard, discussed the key issues related to the exchange and collection of information on branches of credit institutions for macroprudential purposes. The Board exchanged views on an interim report of the Expert Group on Margins and Haircuts, which revisits and extends the previous ESRB findings regarding procyclicality associated with margin and haircut practices. The ESRB will publish this interim report in the coming months and will continue to explore relevant policy options.

Concurrently with this, the ESRB released the 29th issue of its *Risk Dashboard*, in which it is reported that market-based indicators of systemic stress in the EU remained relatively benign despite significant geopolitical and policy uncertainties, highlighting the potential for re-pricing of risks by markets. Economic growth in the EU remained moderate with downside risks to the outlook, while debt levels remain elevated across countries and sectors in the EU – although over the medium-term most countries have deleveraged somewhat. Credit to the private sector continued to grow robustly in many EU Member States, with the cost of borrowing for the private sector remaining low – reflecting the low refinancing costs for banks and the low risk pricing – and, following a period of relative easing, credit standards remained broadly unchanged over the last quarter. Among other things, total assets under management in the EU investment funds and other financial institutions increased in the first quarter of 2019, reflecting a rise in asset valuations following strong declines in the final quarter of 2018.

Separately, on 2 October, the ECB published *Key Vulnerabilities for Euro Area Financial Stability*, the opening remarks by Luis de Guindos, Vice-President of the ECB, at the meeting of the Financial Stability Contact Group. In summary, he states: "We continue to see four key vulnerabilities for euro area financial stability: (i) a risk of mispricing of some financial assets; (ii) high public and private sector indebtedness in several countries; (iii) in view of banks' subdued profitability outlook, we see a risk of hampered bank intermediation capacity; and (iv) vulnerabilities stemming from increased risk taking in the non-bank financial sector. We see the likelihood of these vulnerabilities unravelling in a disorderly manner over the next 18-24 months as remaining largely unchanged. This is because the now widely expected "lower-for-longer" interest rate environment mitigates many of the possible triggers for corrections over the short to medium term."

On 4 October, EBA published its quarterly *Risk Dashboard* covering Q2 data, which summarises the main risks and vulnerabilities in the EU banking sector. Capital ratios have remained broadly stable and banks' asset quality has further improved. However, low profitability keeps on being a key challenge for the sector. Looking forward, rising economic and political uncertainty might negatively affect the EU banking sector; and the challenge of low profitability might aggravate this.

Every year, ECB Banking Supervision – in close cooperation with national supervisors – identifies and assesses the risks faced by euro area banks. The outcome of this exercise, published on 7 October, serves as a basis for defining supervisory priorities and determines focus areas for the regular monitoring and analysis of risks to which supervised banks are exposed. The most important results of the risk assessment exercise are presented in the SSM Risk Map, which shows the key risk drivers that are expected to affect supervised banks over the next two to three years. The three most prominent risk drivers expected to affect the euro area banking system over the next three years are: (i) economic, political and debt sustainability challenges in the euro area, (ii) business model sustainability and (iii) cybercrime and IT deficiencies. These are followed by: execution risk attached to banks' strategies for non-performing loans; easing lending standards; re-pricing in financial markets; misconduct, money laundering and terrorist financing; Brexit; the global outlook and

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Economic growth in the EU remained moderate with downside risks to the outlook, while debt levels remain elevated across countries and sectors in the EU.

geopolitical uncertainties; reaction to regulation; and climate change-related risks.

According to the results of the 2019 supervisory stress test, announced by the SSM on 7 October, the vast majority of banks directly supervised by the ECB have overall comfortable liquidity positions despite some vulnerabilities requiring further attention. The shocks simulated in the exercise were calibrated on the basis of supervisory experience gained in recent crisis episodes, without any reference to monetary policy decisions. The sensitivity analysis focussed solely on the potential impact of idiosyncratic liquidity shocks on individual banks but did not assess the potential causes of these shocks or the impact of wider market turbulence. Supervisors will discuss the conclusions individually with the banks as part of the annual supervisory review and evaluation process. The results will not directly affect supervisory capital requirements but will inform the assessment of banks' governance and liquidity risk management.

On 9 October, the Financial Policy Summary and Record of the Financial Policy Committee Meeting on 2 October 2019 was published, by the Bank of England. Among other things, this reports that the core of the UK financial system including banks, broker dealers and insurance companies is resilient to and prepared for the wide range of risks it could face, including a worst-case disorderly Brexit; and that, reflecting extensive preparations made by UK authorities and the private sector, most risks to UK financial stability that could arise from disruption to cross-border financial services in a no-deal Brexit have been mitigated. It also reports that future shocks to the global economy could be amplified by material debt vulnerabilities, some structural illiquidity in financial markets and reduced space for some monetary authorities to respond; and that the FPC continues to judge that the mismatch between redemption terms and the liquidity of some funds' assets has the potential to become a systemic risk. Additionally, the continued reliance of global financial markets on LIBOR poses risks to financial stability that can be reduced only through a transition to alternative benchmark rates by end-2021.

Published on 11 October, *Interconnectedness and Contagion Analysis: A Practical Framework* is an IMF staff working paper, which offers detailed and practical guidance on how to conduct a comprehensive analysis of interconnectedness and contagion for a country's financial system under various circumstances. The authors survey current approaches at the IMF for analysing interconnectedness within the interbank, cross-sector and cross-border dimensions through an overview and examples of the data and methodologies used in the FSAP. Finally, this paper offers practical advice on how to interpret results and discusses potential financial stability policy recommendations that can be drawn from this type of in-depth analysis.

Also published on 11 October, *A Structural Model of Interbank Network Formation and Contagion* is a Bank of England staff working paper. The authors observe that the interbank network fulfils an important function but may also result in risk propagation. They examine this trade-off by setting out a model in which banks form interbank network links endogenously, taking into account the effect of links on default risk. Estimating this model based on novel, granular data on aggregate exposures between banks, they find that the decentralised interbank market is not efficient: a social planner would be able to increase surplus on the interbank market by 13% without increasing mean bank default risk or decrease mean bank default risk by 4% without decreasing interbank surplus. The authors then propose two novel regulatory interventions – caps on aggregate exposures and pairwise capital requirements – which result in efficiency gains.

Published on 16 October, the latest edition of the IMF's semi-annual *Global Financial Stability Report, Lower for Longer*, identifies the current key vulnerabilities in the global financial system as the rise in corporate debt burdens, increasing holdings of riskier and more illiquid assets by institutional investors, and growing reliance on external borrowing by emerging and frontier market economies. The report proposes that policymakers mitigate these risks through stricter supervisory and macroprudential oversight of firms, strengthened oversight and disclosure for institutional investors, and the implementation of prudent sovereign debt management practices and frameworks for emerging and frontier market economies.

On 22 October, it was announced that, after a highly competitive selection process involving peer reviews by members of the ESRB's Advisory Scientific Committee (ASC), the 2019 Ieke van den Burg Prize for Research on Systemic Risk was jointly awarded to André F. Silva, for his paper entitled *Strategic Liquidity Mismatch and Financial Sector Stability*, and Guillaume Vuillemey, for *Completing Markets with Contracts: Evidence from the First Central Clearing Counterparty*. The ASC also decided to recognise the quality of five additional papers, which are runners-up for the prize.

On 29 October, the ECB published its latest semi-annual *Macroprudential Bulletin*, the aim of which is to raise awareness of macroprudential policy issues in the euro area by bringing greater transparency to the ECB's ongoing work and thinking in this field. In addition to providing an overview of the macroprudential policy measures in the euro area which were in application on 3 October 2019, this edition includes five articles.

The first studies the impact of cyclical systemic risk on future bank profitability for a large sample of EU banks, showing that high levels of cyclical systemic risk lead to large downside risks to bank profitability with a lead time of three to five years. The second contributes to the discussion on the interaction of different regulatory metrics by empirically examining the interaction between the LCR and the NSFR for banks in the euro area, with findings suggesting they are complementary and constrain different types of banks in different ways. The third contributes to the ongoing discussion about the long-term strategy for stress testing in the euro area, highlighting some of the strengths and weaknesses of the constrained bottom-up approach currently used in the EU-wide stress-testing exercise. The fourth investigates the impact of leverage on investor flows in European mutual funds, showing that investors in leveraged funds react more strongly to negative fund performance than investors in unleveraged funds. Finally, the fifth contributes to the ongoing debate on the procyclicality of initial margins in derivative markets and whether the current regulatory framework sufficiently addresses this issue.

On 7 November, the EBA published the final methodology and draft templates for the 2020 EU-wide stress test along with the key milestones of the exercise. The methodology and templates cover all relevant risk areas and incorporate the feedback received during the discussion with the industry in the summer of 2019. The stress test exercise will be formally launched in January 2020 and the results published by 31 July 2020. Similar to the 2018 exercise, the 2020 EU-wide stress test is a bottom-up exercise with constraints, including a static balance sheet assumption; and is

Low interest rates should support economic activity in the euro area but may also encourage excessive risk-taking by some non-bank financial institutions and highly leveraged non-financial corporations.

primarily focused on the assessment of the impact of risk drivers on the solvency of banks. EBA subsequently published the final stress test templates, on 16 December.

Published on 15 November, *Integrating Solvency and Liquidity Stress Tests: The Use of Markov Regime-Switching Models* is an IMF staff working paper, in which the authors present a framework to integrate liquidity and solvency stress tests. An empirical study based on European bond trading data finds that asset sales' haircuts depend on the total amount of assets sold and general liquidity conditions in the market. To account for variations in market liquidity, the study uses Markov regime-switching models and links haircuts with market volatility and the amount of securities sold by banks. The framework is accompanied by a Matlab program and an Excel-based tool, which allow the calculations to be replicated for any type of traded security and to be used for liquidity and solvency stress testing.

Downside risks to global and euro area economic growth have increased and continue to create financial stability challenges, according to the latest ECB *Financial Stability Review* (FSR), published on 20 November. Low interest rates should support economic activity in the euro area but may also encourage excessive risk-taking by some non-bank financial institutions and highly leveraged non-financial corporations, and in some real estate markets. Non-bank financials, which play an increasingly important role in the financing of the real economy, have continued to take on more risk and have increased their exposure to riskier segments of the corporate and sovereign sectors; pockets of vulnerability also remain in the non-financial corporate sector and some property markets; and euro area banks' profitability prospects have deteriorated further, despite expectations of a modest but continued increase in net interest, fee and commission income.

This issue of the FSR contains two special features: (a) euro area bank profitability: where can consolidation help?; and (b) assessing the systemic footprint of euro area banks. It also includes eight boxes: (i) explaining cross-border transactions in euro area commercial real estate markets; (ii) valuations in corporate bond and equity markets; (iii) implications of bank misconduct costs for bank equity returns and valuations; (iv) climate risk-related disclosures of banks and insurers and their market impact; (v) the ECB's new euro area banking sector macro-micro model; (vi) investment funds and the transmission of the global financial cycle to the euro area ; (vii) portfolio rebalancing by euro area investment funds following outflows; and (viii) macroprudential policy and powers within the Eurosystem.

Published on 27 November, *Informality, Frictions, and Macroprudential Policy* is an IMF staff working paper, in which the authors analyse the effects of macroprudential policies through the lens of an estimated dynamic stochastic general equilibrium model tailored to developing markets. In particular, they explicitly introduce informality in the labour and goods markets within a small open economy embedding financial frictions, nominal and real rigidities, labour search and matching, and an explicit banking sector. They use the estimated version of the model to run welfare analysis under optimized monetary and macroprudential rules. Results show that although informality reduces the efficiency of macroprudential policies following a convex fashion, combining the latter with an inflation targeting objective could be beneficial.

On 28 November, ESMA published its latest *Risk Dashboard* for the EU's securities markets, covering the third quarter of 2019. This reports that the market risks remain very high, against the background of a deteriorating growth outlook, continued uncertainty around Brexit, US-China trade tensions and geopolitical risk, with large intra-day movements confirming that markets remain sensitive to the news flow. Risks in markets under ESMA's remit remained high, particularly in securities markets, where high asset valuations and search-for-yield prevail. Credit risk continues to be elevated, with deteriorating corporate debt quality and the growing share of BBB-rated debt as main concerns. Looking ahead, a weakening economic outlook, further uncertainty over global trade negotiations, as well as uncertainty around the Brexit timeline remain key risk drivers.

On 29 November, the EBA published its annual *Report on Risks and Vulnerabilities in the EU Banking Sector*. This is accompanied by the publication of the 2019 EU-wide transparency exercise, which provides detailed information, in a comparable and accessible format, for 131 banks across the EU. Overall, EU banks' solvency ratios remained stable, while the NPL ratio further contracted. Amidst low profitability, a proactive management of operating expenses is essential.

Published on 3 December, *Financial Cycles, Credit Bubbles and Stabilization Policies* is an ECB staff working paper, in which the authors analyse the effects of several policy instruments for mitigating financial bubbles generated in the banking sector. They augment a New Keynesian macroeconomic framework by endogenizing boundedly-rational expectations on asset values of loan portfolios, allow for interbank trading and show how a credit bubble can develop from a financial innovation. They then evaluate the efficacy of several policy instruments in counteracting financial bubbles, finding that an endogenous capital requirement reduces the impact of a financial bubble significantly while central bank intervention proves to be less effective. A welfare analysis ranks the policy reaction through an endogenous capital requirement highest and hence the authors provide a rationale for the use of countercyclical capital buffers.

Published on 6 December, *Sovereign Risk in Macroprudential Solvency Stress Testing* is an IMF staff working paper, in which the authors explain the treatment of sovereign risk in macroprudential solvency stress testing based on the experiences in the FSAP. They discuss four essential steps in assessing the system-wide impact of sovereign risk: scope, loss estimation, shock calibration, and capital impact calculation. Most importantly, a market-consistent valuation approach lies at the heart of assessing the resilience of the financial sector in a tail risk scenario with sovereign distress. They present a flexible, closed-form approach to calibrating haircuts based on changes in expected sovereign defaults affecting bank solvency during adverse macroeconomic conditions. This paper demonstrates the effectiveness of using extreme value theory in this context, with empirical examples from past FSAPs.

On 10 December, FINMA published its risk monitor, which provides an overview of what FINMA believes are the most important risks currently facing supervised institutions and describes the focus of supervisory activity. FINMA currently sees six principal risks for its supervised institutions and the Swiss financial centre: (i) the persistent low interest-rate environment; (ii) a possible correction on the real estate and mortgage market; (iii) cyberattacks; (iv) a disorderly abolition of LIBOR benchmark interest rates; (v) money laundering; and (vi) increased impediments to cross-border market access. FINMA has also identified risks that could have an impact on the Swiss financial centre over the longer term.

Published on 11 December, *Examining Macroprudential Policy and its Macroeconomic Effects – Some New Evidence* is a BIS staff working paper. The authors find that macroprudential policy shocks have effects on real GDP, the price level and credit that are very similar to those of monetary policy shocks, but the detailed transmission of the two policies is different. Whereas macroprudential policy shocks mostly affect residential investment and household credit, monetary policy shocks have more widespread effects on the economy. They also find that positive credit shocks are generally met with tighter macroprudential policy, and macroprudential and monetary policy respond to credit shocks in a complementary way.

Published on 13 December, *Macroprudential Policy Implications of Foreign Branches Relevant for Financial Stability* is an ESRB paper. It reports that although foreign branches vary in size and significance among EU Member States, information on these branches is deemed to be important from a financial stability perspective in a number of EU Member States. EU law allows the exchange of currently available information but does not provide a clear framework for the collection and exchange of currently unavailable information between relevant authorities for macroprudential purposes.

Authorities entrusted with the adoption and/or activation of macroprudential policy measures or other financial stability tasks could be granted access to information on foreign branches, which could be best achieved through a well-designed and efficient voluntary exchange of information based on a mutual agreement between authorities within the existing legal framework. Recommendation ESRB/2019/18, of 26 September, concerns exchange and collection of information for macroprudential purposes on branches of credit institutions having their head office in another Member State or in a third country.

On 16 December, the Bank of England published it latest semi-annual *Financial Stability Report*, setting out the Financial Policy Committee's (FPC's) view on the stability of the UK financial system and what it is doing to remove or reduce any risks to it. This reports that the core of the UK financial system – including banks, dealers and insurance companies – is resilient to, and prepared for, the wide range of UK economic and financial shocks that could be associated with a worst-case disorderly Brexit. Reflecting extensive preparations made by authorities and the private sector, most risks to UK financial stability that could arise from disruption to cross-border financial services in a worst-case disorderly Brexit have been mitigated.

Also, the FPC judges that domestic vulnerabilities (excluding Brexit) that can amplify economic shocks have not changed materially since July and remain at a standard level overall. Looking ahead, irrespective of the particular form of the UK's future relationship with the EU, and consistent with its statutory responsibilities, the FPC will remain committed to the implementation of robust prudential standards in the UK, which will require maintaining a level of resilience that is at least as great as that currently planned – which itself exceeds that required by international baseline standards.

Considering certain market-related topics, the FPC notes that the recent period of volatility in the US dollar repo market shows how markets can become illiquid in the face of shocks and may not be able to rely on dealers to maintain levels of liquidity. Accordingly, investors should not assume that markets will remain liquid at all times. Also, the FPC judges that the mismatch between redemption terms and the liquidity of some funds' assets means there is an advantage to investors who redeem ahead of others, particularly in a stress, which has the potential to become a systemic risk. As part of the ongoing review by the Bank and FCA of open-ended funds, the FPC has established that there should be greater consistency between the liquidity of a fund's assets and its redemption terms.

Separately, continued reliance of financial markets on LIBOR poses a risk to financial stability that can only be reduced through a transition to alternative RFRs, with the intention being that Sterling LIBOR will cease to exist after the end of 2021. Sterling markets show encouraging signs in the development of new products linked to SONIA, and the transition of some legacy products – but important gaps remain, so these efforts will need to continue to accelerate in the first half of 2020.

The Bank also published a *Financial Policy Summary and Record of the Financial Policy Committee Meeting*

Most risks to UK financial stability that could arise from disruption to cross-border financial services in a worst-case disorderly Brexit have been mitigated.

on 13 December 2019; and announced the results of its 2019 stress test of the UK banking system. These results show that the UK banking system is resilient to deep simultaneous recessions in the UK and global economies that are more severe overall than the global financial crisis, combined with large falls in asset prices and a separate stress of misconduct costs. It would therefore be able to withstand the stress and continue to meet credit demand from UK households and businesses.

Losses on corporate exposures are higher than in previous tests, reflecting some deterioration in asset quality and a more severe global scenario. Despite this, and weakness in banks' underlying profitability, all seven participating banks and building societies remain above their hurdle rates. The major UK banks' aggregate CET1 capital ratio after the 2019 stress scenario would still be more than twice its level before the crisis. Major UK banks' capital ratios have remained stable since year-end 2018, the starting point of the 2019 stress test; and at the end of Q3 2019 their CET1 ratios were over three times higher than at the start of the global financial crisis. They also continue to hold sizeable liquid asset buffers.

On 18 December, the Bank of England published a discussion paper, for comment by 18 March, which sets out its proposed framework for the *2021 Biennial Exploratory Scenario* (BES) exercise. The objective of the BES is to test the resilience of the largest banks and insurers to the physical and transition risks associated with different possible climate scenarios, and the financial system's exposure more broadly to climate-related risk. The key features of the BES are multiple scenarios that cover climate as well as macro-variables; broader participation; longer time horizon; counterparty-level modelling; and aggregated output results. The final BES framework will be published in the second half of 2020 and the results of the exercise will be published in 2021.

Published on 20 December, *European Macroprudential Database* is an ECB staff statistics paper. This describes the ECB's Macroprudential Database (MPDB), which is an important component of the ECB's Statistical Data Warehouse. After explaining the rationale for creating the MPDB, the paper illustrates how it supports the macroprudential analysis conducted by the ESCB, the ESRB and the national authorities of the SSM and the EU. The structure of the database and a broad overview of available indicators are then presented, with a description of the relevant confidentiality issues. Examples illustrate how the MPDB is used for monitoring purposes and econometric modelling. Finally, the paper discusses remaining data gaps and expected future enhancements of the database.

Also published on 20 December, *Capital and Liquidity Interaction in Banking* is a Bank of England staff working paper, in which the authors study the interaction between banks' capital and their liquidity transformation in both a theoretical and empirical set-up. They first construct a simple model to develop hypotheses which they test empirically. Using a confidential Bank of England dataset that includes bank-specific capital requirement changes since 1989, they find that banks engage in less liquidity transformation when their capital increases. This finding suggests that capital and liquidity requirements are at least to some extent substitutes. By establishing a robust causal relationship, these results can help guide the optimal joint calibration of capital and liquidity requirements and inform macroprudential policy decisions.

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The transition to risk-free rates: other recent publications

RFR

In addition to the feature article in this Quarterly Report, there have also been several other publications of note relating to the transition to risk-free rates generally:

- In July 2019, IOSCO published a statement setting out matters for market participants to consider if they have exposure to LIBOR, particularly USD LIBOR, in light of its expected cessation after the end of 2021 and USD LIBOR's widespread global use. The key messages from the statement were: RFRs provide a robust alternative to IBORs and can be used in the majority of products; in both new and existing IBOR contracts, the inclusion of robust fallbacks should be considered a priority; the best risk mitigation to a LIBOR cessation event is moving to RFRs now; and it is prudent risk management for market participants to engage early in the LIBOR transition process in preparation for the cessation of LIBOR post-2021.
- The SEC published a staff statement in July 2019 on LIBOR transition encouraging market participants to manage transition away from LIBOR and providing guidance in specific areas.
- Also in July 2019, the ECB published an updated version of its *Explainer on Benchmark Rates*. It also sent a Dear CEO Letter to significant institutions requesting a board-approved summary of key risks relating to benchmark reform and a detailed action plan to mitigate such risks, address pricing issues and implement process changes, as well as contact points at management level who are in charge of overseeing the implementation of these action plans.
- In September 2019, the Bank of England published an analysis entitled *How Prepared are the Markets for the End of LIBOR?*. The analysis had been presented to the Bank of England Financial Policy Committee (FPC) in June 2019.
- The ARRC updated its previously released set of frequently asked questions (FAQs) in September 2019. The FAQs are updated from time to time to reflect developments, provide information about the work of ARRC, its progress to date, and the overall effort to promote voluntary market adoption of SOFR.
- In September 2019, the ARRC released a practical implementation checklist to help market participants transition to using SOFR. The information in the checklist was expected to be especially helpful for market participants that have not fully started taking the steps needed to transition away from LIBOR.
- Also in September 2019, the Executives' Meeting of East Asia-Pacific (EMEAP) Working Group on Financial Markets released a *Study on Implications of Financial Benchmark Reforms*, which aims to raise market awareness and further enhance market readiness for financial benchmark reforms. The study focuses on the implications of LIBOR discontinuation, the EU BMR and reform of local benchmarks in the EMEAP region.
- The record of the Bank of England's FPC meeting of 2 October 2019 stressed the importance of accelerating the transition away from LIBOR to alternative reference rates and noted that, in Q4 2019, the FPC would consider further potential policy and supervisory tools that could be deployed by authorities to reduce the stock of legacy LIBOR contracts to an irreducible minimum ahead of end-2021.
- To enable a smooth transition from EONIA to €STR, the Euro RFR Working Group made available a communication toolkit, providing material which interested parties can use in their own communication and education efforts. The toolkit currently consists of: (i) frequently asked questions dated 17 October 2019; (ii) a standard set of slides; and (iii) a checklist.
- In October 2019, the Euro RFR Working Group published its report on *Risk Management Implications of the Transition from EONIA to the €STR and the Introduction of €STR-based Fallbacks for EURIBOR*. The report focuses mainly on the risk management implications for banks, but also touches on additional challenges facing the asset management and insurance sectors. It should be read in conjunction with *Recommendations of the Working Group on Euro Risk-Free Rates on the EONIA to €STR Legal Action Plan* and *Report by the Working Group on Euro Risk-*

Free Rates on the Impact of the Transition from EONIA to the €STR on Cash and Derivatives Products.

- The Hong Kong Monetary Authority (HKMA) published a letter on 23 October 2019 addressed to relevant authorised institutions providing an overview and status update on the transition from IBORs to alternative reference rates. It states that the Treasury Markets Association has identified the Hong Kong Dollar Overnight Index Average (HONIA) as the alternative reference rate to the Hong Kong Interbank Offered Rate (HIBOR) and there is no plan to discontinue HIBOR. In addition, HKMA observes that many authorised institutions have made progress in preparing for the transition to alternative reference rates. To monitor progress, the HKMA will start conducting regular surveys and take suitable follow up actions.
- In November 2019, ICE Benchmark Administrator published a feedback statement on possible enhancements to the ICE Swap Rate (the principal global benchmark for swap rates and spreads for EUR, GBP and USD interest rate swaps). IBA intends to seek to: expand the data used in the ICE Swap Rate calculation and work with ISDA on potential fallbacks; work to produce ICE Swap Rates based on SONIA; and consider the introduction of ICE Swap Rates based on other risk-free rates in due course.
- Also in November 2019, EMMI confirmed that it has successfully completed the phase-in of all panel banks to the EURIBOR hybrid methodology. The phase-in, which began in Q2 2019, occurred on a gradual basis in order to minimise operational and technological risks for panel banks, EURIBOR users, and the benchmark itself.
- The Working Group on Sterling Risk-Free Reference Rates opened invitations to join three new task forces focusing on (i) frameworks to support transition of legacy cash products, (ii) providing market input regarding the "tough legacy" products that may prove unable to be converted or amended to include robust fallbacks and (iii) enablers to moving new loans issuance away from GBP LIBOR.
- The Financial Stability Board published its annual progress report on implementation of recommendations to reform major interest rate benchmarks in December 2019. The report emphasises that the continued reliance of global financial markets on LIBOR poses risks to financial stability and calls for significant and sustained efforts by the official sector and by financial and non-financial firms across many jurisdictions to transition away from LIBOR by end-2021.
- FINMA published a *Risk Monitor Report* in December 2019 that identifies the six most important risks currently being faced by Swiss financial institutions. It includes the discontinuation of LIBOR and details three specific risks: legal risk, valuation risk and the risk related to related to operational readiness. The report states that FINMA-mandated self-assessments indicate that most banks are behind schedule and cautions of the far-reaching consequences of inadequate preparation for the transition to SARON.
- In its *Semi-Annual Risk Perspective Report* published in December 2019, the United States Office of the Comptroller of the Currency noted that it would be increasing regulatory oversight in relation to the discontinuation of LIBOR to evaluate bank awareness and preparedness for LIBOR's anticipated cessation.

Further general publications, including regular newsletters from official sector working groups, are made available on the following webpages:

- FSB information and materials
- ECB information and materials
- ESMA information and materials
- Financial Conduct Authority information and materials
- £RFR Working Group information and materials
- Alternative Reference Rates Committee information and materials
- Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks information and materials
- Euro RFR Working Group information and materials
- The National Working Group on Swiss Franc Reference Rates information and materials

In addition, ICMA seeks to include links to relevant publications on its benchmark reform and transition to risk-free rates webpage.

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Credit rating agencies

On 8 October 2019, the Joint Board of Appeal of the ESAs published its decision in the appeal by the German credit rating agency, Creditreform AG, against the EBA. Creditreform appealed, on 16 July 2019, challenging the adoption by the Joint Committee of the ESAs of certain draft ITS proposed for endorsement by the European Commission; and made an application for suspension. The draft ITS proposed to amend the correspondence (mapping) between certain of Creditreform's long-term corporate credit assessments and certain credit quality steps as set out in the CRR. The Board of Appeal dismissed the appeal as inadmissible, in accordance with settled case law of the CJEU.

On 29 November, ESMA published its annual market share calculation for EU registered CRAs for 2019. The results show that the three largest CRAs – S&P Global Ratings, Moody's Investor Service and Fitch Ratings – account for 92.1% of the market for CRAs in the EU representing a 2.7% increase on 2018. The remaining 7.9% of the market is shared between 23 registered CRAs. The annual market share calculation also provides a breakdown of the type of ratings offered by each registered CRAs as well as the proportion of ratings for EU debt issuances by asset class.

On 5 December, ESMA launched a consultation, for comment by 16 March, on proposed *Guidelines on Internal Controls for CRAs*, which sets out the systems and controls that CRAs should have in place to meet the requirements of the CRA Regulation (CRAR) on internal controls. These guidelines set out the criteria that CRAs should have in place, focusing on their internal controls framework and functions, to demonstrate to ESMA that adequate and effective internal control systems exist to ensure the accuracy and integrity of the credit rating process.

On 13 December, ESMA opened a public consultation, for comment by 18 January, on future procedural rules regarding penalties for third country (TC) CCPs, trade repositories (TRs) and CRAs. The consultation deals with specific aspects of the procedural rules for imposing fines and penalties to TC-CCPs, TRs and CRAs, with the aim of aligning the three sets of rules. ESMA seeks views on a future technical advice on the rules to impose penalties and fines on TC-CCPs, TRs and CRAs, which builds on the existing enforcement framework regarding TRs and CRAs as well as on ESMA's supervisory experience gained in recent years.

On 20 December, ESMA published a *Follow Up to the Thematic Report on Fees Charged by CRAs and Trade Repositories (TRs)*. This report, building on 2018's thematic work, highlights good practices implemented by CRAs and TRs in the areas of fee transparency, fee setting and costs monitoring. It finds that CRAs should further improve the transparency of their pricing and their fee setting process, to ensure that fees are non-discriminatory and based on actual costs. ESMA also finds that CRAs need to improve access to and usability of the credit ratings published on their websites and that they should remain responsible for overseeing the distribution of the credit ratings they produce. ESMA will monitor how supervised firms develop their practices and assess whether their implementation is compliant with the regulatory requirements on fees. ESMA will also carry out further work to improve access to and use of credit ratings.

On 14 November, ESMA announced its withdrawal of the CRA registration of DG International Ratings SRL (previously Dagong Europe Credit Rating Srl) (DG International). This decision follows official notification sent to ESMA by DG International, on 25 October, of its intention to renounce its registration as a CRA under the conditions set out in Article 20(1)(a) of the CRA Regulation (CRAR).

Following this latest change, the total number of CRAs registered in the EU is 27 CRAs – amongst which four operate under a group structure, totaling 18 legal entities in the EU, which means that the total number of CRA entities registered in the EU is 41. In addition, there are four CRA's certified in accordance with the EU CRA Regulation.

The most recent update to ESMA's Q&A on the application of the EU CRA Regulation was published on 18 December 2018.

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OTC (derivatives) regulatory developments

On 3 October 2019, ESMA published a consultation paper, for comment by 2 December, on draft technical advice to the European Commission on specifying the conditions under which commercial terms are to be considered fair, reasonable, non-discriminatory and transparent (FRANDT) where clearing service providers offer clearing services to clients. During the implementation of EMIR's clearing obligation, several counterparties have experienced issues around access to clearing, in response to which EMIR Refit has introduced a number of measures to address it – including the FRANDT requirements. The consultation sets out the requirements for FRANDT commercial terms, based on the four criteria listed under Article 4(3a) of EMIR, namely: fairness and transparency; unbiased and rational contractual arrangements; to facilitate clearing services and prices to be fair and non-discriminatory; and risk control criteria.

On 4 October, ESMA launched a consultation, for comment by 22 November, on possible amendments to the trading obligation under MiFIR following the introduction of EMIR Refit. Recent changes to EMIR, via Refit, modify the scope of counterparties subject to the clearing obligation – exemption for small financial counterparties and modified determination of non-financial counterparties – but this has not been accompanied by direct amendments to MiFIR, which currently leads to a misalignment between the scope of counterparties subject to the clearing obligation (CO) under EMIR and the derivatives trading obligation (DTO) under MiFIR. ESMA's consultation proposal is to formulate a recommendation to the European Commission to align these.

On 15 October, the FSB published its annual progress report on the implementation of the agreed G20 reforms to OTC derivatives markets. Overall there has been limited additional implementation of the reforms between end-November 2018 and end-September 2019. The report notes the following progress:

(i) trade reporting: 23 out of 24 member jurisdictions have comprehensive requirements in force, an increase of one during the reporting period;

(ii) central clearing: eighteen jurisdictions have in force comprehensive standards/criteria for determining when standardised OTC derivatives should be CCP cleared;

(iii) margin requirements: sixteen jurisdictions have in force comprehensive margin requirements for non-CCP cleared derivatives, which represents an increase of one during the reporting period;

(iv) higher capital requirements for non-CCP cleared derivatives: interim higher capital requirements for non-CCP cleared derivatives are in force in 23 of the 24 FSB member jurisdictions;

(v) platform trading: comprehensive platform trading requirements are in force in 13 jurisdictions, a number which has remained unchanged during the reporting period; and

(vi) cross-border coordination and issues: one jurisdiction started exercising deference during the reporting period with regard to foreign jurisdictions' regimes.

On 11 November, ESMA published three sets of technical advice to the European Commission regarding third country (TC) CCPs under EMIR 2.2. ESMA's advice details: how to specify the criteria to determine whether a TC-CCP is systemically important for the EU or a Member State's financial stability (tiering); how to assess comparable compliance; and the fees to be charged to TC-CCPs. ESMA has sent its advice to the Commission for the development of the corresponding Delegated Acts, on which the Commission will consult publicly before it finalises them.

On 4 December, it was announced that the Board of Supervisors of ESMA has appointed Robert Ophèle, the Chair of the Autorité des Marchés Financiers (AMF) of France, as the Acting Chair of ESMA's CCP Supervisory Committee – which is being established as part of the reform of the current regime for the authorisation, recognition and supervision of CCPs under EMIR 2.2. The appointment is effective from 1 January 2020, when the CCP Supervisory Committee's work is expected to begin, with the Acting Chair responsible for ensuring the set-up and functioning of the Committee, pending the appointment of a full-time Committee Chair.

On 5 December, the ESAs published joint draft RTS to amend the Delegated Regulation on the risk mitigation techniques for non-cleared OTC derivatives (bilateral margining) as well as a joint statement on the introduction of fallbacks in OTC derivative contracts and the requirement to exchange collateral. Both RTS and the statement were developed to facilitate further international consistency in the implementation of the global framework agreed by the BCBS and IOSCO.

On 9 December, ESMA published its second *Annual Statistical Report* analysing the EU derivatives markets. This report, based on data submitted under EMIR, provides a comprehensive market-level view of the EU's derivatives markets in 2018, which had a total size of €735 trillion gross notional amount outstanding, an increase of 11% on 2017. The growth in this market is driven by an increase in interest rate derivatives and equities, which make up respectively 76% and 6% of the total. OTC trading continues to account for the majority of the trading in derivatives and, across all asset classes, exposures are highly concentrated in relatively few counterparties.

On 9 December, ESMA published its second annual report regarding supervisory measures carried out and penalties imposed by NCAs under EMIR. This report, covering the period from January to December 2018, focuses on NCAs supervisory measures and enforcement actions, their powers and the interaction between NCAs and market participants, when monitoring compliance with the following EMIR requirements: the clearing obligation for certain OTC derivatives; the reporting obligation of derivative transactions to TRs; requirements for non-financial counterparties; and risk mitigation techniques for non-cleared OTC derivatives. The report highlights that some supervisory areas are highly harmonised but also identifies areas of supervisory challenge which might benefit from coordinated approaches.

On 12 December, Regulation (EU) 2019/2099 (EMIR 2.2), amending EMIR as regards the procedures and authorities involved for the authorisation of CCPs and requirements for the recognition of third-country CCPs, was published in the EU's Official Journal. It enters into force on the 20th day following this publication.

Published on 17 December, *Interdependencies in the Euro Area Derivatives Clearing Network: A Multi-layer Network Approach* is an ECB staff working paper. The authors note that the global nature of derivatives markets, and the presence of large key financial institutions trading in several markets across the globe, call for taking a "macro" view on the interconnections arising in the clearing network. Based on the analysis of derivatives transactions data reported under the EMIR Regulation they reconstruct the network of relationships in the CCP-cleared derivatives market and analyse its topology providing insight into its structural features.

The CCP-cleared derivatives network is modelled in the form of a multiplex network where each layer is represented by a derivatives asset class market. In turn, each node represents a single counterparty in that market. On the basis of different centrality measures applied to the collapsed aggregate and to the multiplex network, the critical participants of the euro area CCP-cleared derivatives market are identified and their level of interconnectedness analysed. This paper provides insight on how the collected data pursuant to the EMIR Regulation can be used to shed light on the complex network of interrelations underlying the financial markets. It provides indications on structural features of the euro area CCP-cleared derivatives market and discusses policy relevant implications and future applications.

On 23 December, ESMA announced that it has extended the recognition decisions for the three CCPs established in the UK, to reflect the extension of the expiry date of the *Implementing Decision (EU) 2018/2031* of the European Commission on the equivalence of the UK CCP legal framework. These recognition decisions would take effect on the date following Brexit date, under a no-deal Brexit scenario.

In view of ESMA's statutory role to build a common supervisory culture by promoting common supervisory approaches and practices, ESMA has established a process for adopting Q&A documents which relate to the consistent application of EMIR. The first version of ESMA's EMIR Q&A document was published on 20 March 2013, with the most recent update having been published on 7 January.

ESMA's list of CCPs authorised to offer services and activities in the EU, in accordance with EMIR, was last updated on 12 November; its list of third-country CCPs recognised to offer services and activities in the EU was last updated on 3 December; but its (non-exhaustive) list of CCPs established in non-EEA countries which have applied for recognition has not been updated since 24 January. ESMA's *Public Register for the Clearing Obligation* under EMIR has not been updated since 6 December 2018, while its public register of those derivative contracts that are subject to the trading obligation under MiFIR was last updated on 3 October.

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Market infrastructure

ECB: Advisory Groups on market infrastructure

The ECB's Advisory Group on market infrastructure for securities and collateral (AMI-SeCo) brings together senior experts from banks and market infrastructures to feed into the ECB's work in relation to market infrastructure. This includes new initiatives but also the operation of existing platforms, particularly of course TARGET2-Securities, the Eurosystem's common settlement platform. The ICMA ERCC is represented in the group through Nicholas Hamilton, chair of the ERCC Operations Group. The latest meeting of AMI-SeCo was held on 5 December in Frankfurt. The AMI-SeCo meeting itself was preceded by a joint session with the ECB's other infrastructure advisory group, the AMI-PAY, which is being organised on an annual basis. The shorter joint session which was held on 4 December was an opportunity to cover some of the overarching topics that impact both groups. This year the meeting focused on two main themes: the ECB's ongoing work to consolidate the TARGET2 (T2) and T2S platforms and a few related questions, as well as the ECB's work in relation to FinTech and whether this needs to be extended to payments.

The following day, AMI-SeCo members focused in more detail on the securities-specific aspects of the infrastructure work. They reviewed the latest developments in T2S operations, including settlement volumes and efficiency. Members also focused on the remaining ECB initiatives in the area of market infrastructure, other than the T2-T2S consolidation, including the Eurosystem Collateral Management System (ECMS) and the extensive related collateral management harmonisation work (both of which covered more in detail below). At the meeting, the ECB also shared a first summary of the feedback received in response to a public consultation over summer on the EDDI initiative, the ECB's proposal to establish a centralised platform for the issuance and initial distribution of debt instruments. Unfortunately, no documents and presentations from the meetings are available yet, but they should be published in due course on the AMI-SeCo documents page.

ECB: ECMS and collateral management harmonisation

One of the key priorities for AMI-SeCo continues to be the ongoing work in relation to collateral management harmonisation. This work is coordinated by a dedicated Task Force on Collateral Management Harmonisation (CMH-TF), which includes several members of the ERCC Operations Group, who have been actively contributing to the different CMH-TF work streams. Since its launch in early 2017, the main focus of the CMH-TF has been on three specific areas of harmonisation: (i) triparty collateral management, (ii) corporate actions, and (iii) CSD billing. These issues had been identified as an important pre-condition for the development of the Eurosystem Collateral Management System (ECMS), which is due to go live in November 2022. Detailed harmonisation standards have been developed by the CMH-TF for all three areas and since then endorsed by AMI-SeCo. They are currently being implemented in close coordination with National Stakeholder Groups (NSGs).

With those standards finalised, the focus of the CMH-TF has now shifted to the seven remaining collateral management activities where members had previously identified some potential for harmonisation on the way to a Single Collateral Management Rulebook for Europe. Four expert groups have been set up to help progress the work in their respective focus areas, namely: (i) bilateral collateral management, including margin calls, settlement cut-off times and sourcing of collateral, (ii) triparty collateral management, including questions related to the development of a single triparty model and a focus on messaging, (iii) asset servicing, including issues related to corporate actions (focus on equities), and (iv) taxation processes.

Since then all the expert groups have held regular conference calls, reporting back on progress to the CMH-TF, most recently at the latest meeting on 12 November. As part of the work of the expert groups, ICMA had been asked to look more closely at settlement cut-off times, updating the results from a 2014 survey on the same topic. Over the summer ICMA, jointly with ISLA, sent out an updated survey to members and received responses from over 40 firms. The aggregated results were presented to the CMH-TF on 12 November. Overall, the results show that there has been significant progress over the past years since the previous survey.

Another issue that continues to be discussed within the CMH-TF (and also at the latest AMI-SeCo meeting) is the migration to ISO20022 messaging which has been proposed as part of the harmonisation standards for corporate actions and billing processes. The proposal foresees a staggered implementation approach in two waves. According to the plan, a first wave of parties directly involved in Eurosystem credit operations (ICSDs, NCBs and Eurosystem counterparties) would move to ISO20022 messaging in November 2022, whereas all remaining relevant actors/account servicers would commit to implement ISO20022 messaging by November 2025. The previous message formats based on ISO15022 will continue to be available thereafter during a transition period but will be fully deactivated in November 2028.

ECB: other market infrastructure-related developments

The overall responsibility of the Eurosystem's market infrastructure work, including the operation of existing platforms (T2, T2S and TIPS) and other infrastructure related projects, lies with the ECB's Market Infrastructure Board (MIB). Earlier this year the composition of the MIB changed quite significantly, with the departure of three members (including its Chair, Marc Bayle). In September, the ECB published an overview of the changes, including some interesting thoughts from departing and new members.

On 14 November, at their annual Collateral Conference in Brussels, Euroclear officially announced that Euroclear Bank is intending to join the T2S platform in order to offer participants direct access to both commercial and central bank money settlement. This is clearly an important step in the evolution of T2S, although the full details of the proposal and the associated timeline are yet to be released.

The TARGET Instant Payment Settlement (TIPS) service was launched by the Eurosystem in November 2018 to enable payment service providers to offer fund transfers to their customers in real time. Since its launch over a year ago, the list of connected banks has continued to grow. The full list of reachable parties in TIPS is available on the ECB website.

ECB: market contact groups

Members of the ECB's Bond Market Contact Group (BMCG) had their latest meeting on 20 November. The agenda of the meeting included three main topics. As usual members discussed the bond market outlook, reviewing recent developments but also looking ahead to the year-end. This agenda item was introduced by Union Investment. A second item on the agenda was market and survey-based inflation expectations. EFAMA and the ECB introduced a discussion on this topic, reviewing existing measures of inflation expectations, as well as their uses and respective shortcomings. The third focus of the meeting was on algorithmic trading in bonds markets, including the latest trends and developments, based on presentations by Citi and Morgan Stanley. A more detailed summary of the meeting is available on the BMCG webpage. The next regular meeting of the group has been scheduled for 4 March 2020.

The latest meeting of the Money Market Contact Group (MMCG) was held on 3 December. At the meeting members reviewed the latest developments in euro money markets and expectations for the upcoming year-end. This included discussions on the initial impacts of the new two-tiered system of remunerating central bank reserves, introduced by the ECB in October, repo market conditions ahead of the year-end and the money market outlook for 2020. As part of the agenda, members also discussed recent developments in short-term securities issuance, based on a joint presentation by Bayerische Landesbank and Natixis. During the meeting, the ECB also presented a first summary of the feedback received in response to the EDDI consultation which was held over summer. Finally, members also exchanged views on the recent transition to €STR, the euro area's new risk-free reference rate. Presentations from the meeting will be made available shortly. Members of the MMCG will reconvene for the next meeting on 24 March 2020.

ESMA: post-trading

On 31 October, ESMA published updated validation rules for SFTR reporting. The validation rules were published alongside a set of XML schemas for reporting, also referred to as usage guidelines or derived messages. The schemas specify standardised message formats for SFTR derived from the related ISO messages. While these two documents are important, the most important part of the SFTR Level 3 measures, namely the Reporting Guidelines, was delayed. On 6 January 2020, ESMA finally published the full set of remaining Level 3 measures including the final Guidelines.

ESMA also has an important role to play in the implementation of CSDR. The most recent addition to the list of implementation measures was a set of *Guidelines on Standardised Procedures and Messaging Protocols* under CSDR Article 6(2) which was published on 8 October. ESMA also maintains a growing list of Q&As on CSDR implementation. The document was last updated on 3 December and now covers 20 questions across the four main areas of CSDR requirements. The authorisation process for CSDs under the new harmonised legal framework is still under way. While national competent authorities are in charge of the authorisation itself, ESMA is monitoring the process and maintains a register of all newly authorised CSDs. Since the previous edition of the Quarterly Report, two further CSDs have received their CSDR authorisation, Euroclear Sweden on 14 November and Euroclear Bank on 4 December, which means that 17 CSDs in total have been authorised under CSDR so far.

As a related but separate task, ESMA also maintains the register for payment and securities settlement systems that have been designated by Member States under the Settlement Finality Directive, which was last updated on 23 September.

ESMA also maintains similar registers for the authorisation of CCPs under EMIR, which have also recently been updated. This includes the actual register of EU CCPs authorised under EMIR, which lists a total of EU 16 CCPs, but also a list of third-country CCPs which have been recognised to provide services in the EU, which, with the most recent addition of Multi Commodity Exchange Clearing Corporation of India, now includes 34 CCPs in total.

Another important priority under EMIR, besides the authorisation and supervision of CCPs, is the extensive transaction reporting regime for derivatives. On 17 October, ESMA published a detailed peer review on data quality under EMIR published. In total, a selection of six NCAs participated in the process. Results differ quite significantly between the NCAs assessed but are generally rather mixed. The full report is available on the ESMA website.

BIS: Committee on Payments and Market Infrastructures (CPMI)

Jointly with IOSCO, the CPMI continues to develop a globally harmonised framework for unique identifiers and other data elements for regulatory reporting. This work covers Unique Trade Identifiers (UTIs), Unique Product Identifiers (UPIs), and other critical data elements for OTC derivatives. The latest report in this context was published on 9 October, focusing on *Governance Arrangements for Critical OTC Derivatives Data Elements (other than UTI and UPI)*. While currently focused on OTC derivatives reporting, many aspects will be relevant for other asset classes too, in particular SFTs.

CPMI-IOSCO are responsible for monitoring the implementation of the 2012 *Principles of Financial Market Infrastructures* (PFMI), a set of international standards for payment systems, CSDs and securities settlement systems, CCPs and trade repositories. Besides the many recommendations for FMIs, the PFMI also sets out five key responsibilities for central banks and market regulators in the relevant jurisdictions. This includes Responsibility E on the cooperation with other authorities. On 10 December, CPMI-IOSCO published a detailed review focusing on this responsibility. The report describes the various ways in which authorities cooperate to implement the PFMIs, including use cases and lessons learnt across the different FMI types.

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FinTech in International Capital Markets


by Gabriel Callsen and Rowan Varrall

FinTech regulatory developments

European Commission: consultation on EU framework for markets in crypto-assets

On 19 December 2019, the European Commission launched a *Consultation on an EU Framework for Markets in Crypto-Assets*. Building on the advice from the EBA and ESMA, this consultation should inform the Commission services' ongoing work on crypto-assets: (i) for crypto-assets that are covered by EU rules by virtue of qualifying as financial instruments under MiFID II or (ii) as electronic money/e-money under the Electronic Money Directive (EMD II), the Commission services have screened EU legislation to assess whether it can be effectively applied. For crypto-assets that are currently not covered by the EU legislation, the Commission services are considering a possible proportionate common regulatory approach at EU level to address, *inter alia*, potential consumer/investor protection and market integrity concerns. The consultation is open until 19 March 2020.

European Commission: consultation on a digital operational resilience framework for financial services

On 19 December 2019, the European Commission also launched a *Consultation on a Digital Operational Resilience Framework for Financial Services: Making the EU Financial Sector More Resilient and Secure*. The EU has taken steps towards a horizontal cyber security framework that provides a baseline across sectors. The ICT and security risks faced by the financial sector and its level of preparedness and integration at EU level warrant specific and more advanced coordinated actions that build on, but go substantially beyond, the horizontal EU cyber security framework and that are commensurate with a higher degree of digital operational resilience and cyber security maturity expected from the financial sector. The focus of this public consultation is to inform the Commission on the development of a potential EU cross-sectoral digital operational resilience framework in the area of financial services. This consultation aims at gathering all stakeholders' views in particular on: strengthening the digital operational resilience of the financial sector, in particular as regards the aspects related to ICT and security risk; the main features of an enhanced legal framework built on several pillars; the impacts of the potential policy options. The consultation is open until 16 March 2020.

ECB: exploring anonymity in central bank digital currencies

On 17 December 2019, the ECB released its "In Focus" paper (issue no. 4), *Exploring Anonymity in Central Bank Digital Currencies*. Against the background of the ongoing digitalisation of the economy, the payments ecosystem needs to find an answer to an issue that concerns all citizens: the question of how to allow some degree of privacy in electronic payments, while still ensuring compliance with AML/CFT regulations. The proof of concept that has been developed by the ESCB's EUROchain research network proposes an answer to that question for CBDC. The EUROchain research network seeks to foster a common understanding of DLT and gain practical experience of such technology. The main thing that this prototype shows is that, in a simplified environment typical of a proof of concept, DLT can be used to balance an individual's right to privacy with the public's interest in the enforcement of AML/CFT regulations.

European Commission Expert Group: report on regulatory obstacles to financial innovation

On 13 December 2019, the European Commission's Expert Group on Regulatory Obstacles to Financial Innovation (ROFIEG) published its recommendations on creating an accommodative framework for FinTech in the EU. Although the ROFIEG does not identify many obstacles in existing EU law, the group highlights that the absence of EU law, the inconsistent application of EU law, and the gap in supervisory knowledge in various areas is hampering the scaling up of FinTech in the EU. The ROFIEG also recommends action to further empower data subjects as regards access to and sharing of data. The ROFIEG has used as guiding principles the need for "technological neutrality" in regulatory and supervisory approaches (same activity, same risk, same rule). The ROFIEG also urges a cross-sectoral and, where relevant, internationally coordinated approach in view of the potential application of FinTech across the financial sector.

CPMI: considerations for developers of wholesale digital tokens

On 12 December 2019, the CPMI issued a report setting out a list of criteria for developers and market participants to consider when designing digital tokens for use in wholesale transactions. The *Wholesale Digital Tokens* report describes the potential innovations and design questions associated with digital tokens that could be used to settle wholesale, or large-value, payments, made possible by new technologies such as blockchain, or distributed ledger technology. Private developers are exploring several applications for wholesale digital tokens. While these could be developed simply to make payments, many initiatives also seek to provide the payment leg of tokenised securities and FX transactions, where a token represents a share, bond or other financial asset. The report only covers variants of digital tokens issued by identifiable issuers and denominated in sovereign currency. It is not directed at so-called "stablecoins" for retail payments.

BCBS: designing a prudential treatment for crypto-assets

On 12 December 2019, the BCBS published a discussion paper to seek the views of stakeholders on a range of issues related to the prudential regulatory treatment of crypto-assets, including: (i) the features and risk characteristics of crypto-assets that should inform the design of a prudential treatment for banks' crypto-asset exposures; and (ii) general principles and considerations to guide the design of a prudential treatment of banks' exposures to crypto-assets, including an illustrative example of potential capital and liquidity requirements for exposures to high-risk crypto-assets. The Committee welcomes comments on the analyses and ideas set out in this paper from all stakeholders, including academics, banks, central banks, finance ministries, market participants, payment system operators and providers, supervisory authorities, technology companies and the general public. Comments on any element of this discussion paper should be submitted by 13 March 2020.

DLT can be used to balance an individual's right to privacy with the public's interest in the enforcement of AML/CFT regulations.

FSB: financial stability implications of BigTech in finance

On 9 December 2019, the FSB published the report *BigTech in Finance: Market Developments and Potential Financial Stability Implications*. The entry of BigTech firms into finance has numerous benefits. They can also contribute to financial inclusion, particularly in emerging markets and developing economies, and may facilitate access to financial markets for small and medium-sized enterprises. However, BigTech firms may also pose risks to financial stability. Some risks are similar to those from financial firms more broadly, stemming from leverage, maturity transformation and liquidity mismatches, as well as operational risks. The financial services offerings of BigTech firms could grow quickly given their significant resources and widespread access to customer data, which could be self-reinforcing via network effects. An overarching consideration is that a small number of BigTech firms may in the future come to dominate, rather than diversify, the provision of certain financial services in some jurisdictions.

FSB: third party dependencies in cloud services

On 9 December 2019, the FSB also released the publication *Third-Party Dependencies in Cloud Services: Considerations on Financial Stability Implications*. The adoption of cloud computing and data services across a range of functions at financial institutions raises new financial stability implications. By creating geographically dispersed infrastructure and investing heavily in security, cloud service providers may offer significant improvements in resilience for individual institutions and allow them to scale more quickly and to operate more flexibly. However, there could be issues for financial institutions that use third-party service providers due to operational, governance and oversight considerations, particularly in a cross-border context and linked to the potential concentration of those providers. The report concludes that there do not appear to be immediate financial stability risks stemming from the use of cloud services by financial institutions. However, there may be merit in further discussion among authorities.

IMF: designing central bank digital currencies

On 18 November 2019, the IMF issued the *Working Paper (QP/19/252), Designing Central Bank Digital Currencies*. The paper studies the optimal design of a central bank digital currency (CBDC) in an environment where agents sort into cash, CBDC and bank deposits according to their preferences over anonymity and security; and where network effects make the convenience of payment instruments dependent on the number of their users. CBDC can be designed with attributes similar to cash or deposits and can be interest-bearing: a CBDC that closely competes with deposits depresses bank credit and output, while a cash-like CBDC may lead to the disappearance of cash. Then, the optimal CBDC design trades off bank intermediation against the social value of maintaining diverse payment instruments. When network effects matter, an interest-bearing CBDC alleviates the central bank's trade-off.

BIS: innovation hub centre in Singapore

On 13 November 2019, the MAS and the BIS launched the BIS Innovation Hub Centre in Singapore. This is the BIS's first expansion of its global footprint in 17 years. The Hub Centre in Singapore will initially focus on two projects. The first project is to establish a framework for public digital infrastructures on identity, consent and data sharing. Trusted digital identities for individuals and corporates is a foundational public good that supports the development of inclusive digital financial services including payments as well as other transactions in the broader digital economy. The second project is to create a digital platform connecting regulators and supervisors with digital and technology solution providers. Through the platform, central banks can put up regulatory problems and challenges to source solutions from the FinTech community. This will help central banks develop innovative solutions and policies for cost-effective regulation and supervision.

IOSCO: statement on IOSCO study of emerging global stablecoin proposals

On 4 November 2019, IOSCO issued a statement on its study of emerging global stablecoin proposals. In 2019, IOSCO examined a number of ["stablecoin"] initiatives. The IOSCO Board acknowledged that stablecoins can potentially offer benefits to market participants, consumers and investors. However, the IOSCO Board is also aware of potential risks in a number of areas, including consumer protection, market integrity, transparency, conflicts of interest and financial crime, as well as potential systemic risks. To support its discussions, the IOSCO FinTech Network produced an assessment for the Board of how IOSCO Principles and Standards could apply to global stablecoin initiatives. The detailed assessment concluded that a case-by-case approach is needed to establish which IOSCO Principles and Standards, and national regulatory regimes, would apply. A detailed understanding of how the particular proposed stablecoin is expected to operate is therefore needed, including the rights and obligations it confers on participants and the continuing obligations of the sponsor.

EBA: potential impediments to the cross-border provision of banking and payment services

On 29 October 2019, the EBA published a report identifying potential impediments to the cross-border provision of banking and payment services in the EU. The first important challenge is the identification of when a digital activity is to be regarded as a cross-border provision of services. Although this is a crucial element in determining which regulatory and supervisory frameworks apply, currently, competent authorities and firms lack clear guidance on how to classify cross-border activity under the freedom to provide services or right of establishment. The second challenge stems from areas of EU law that are not fully harmonised or are not yet covered by EU law. In particular, the EBA identifies issues related to authorisations and licensing, consumer protection, conduct of business requirements and anti-money laundering (AML) and countering the financing of terrorism (CFT).

G7 Working Group on Stablecoins: investigating the impact of global stablecoins

On 18 October 2019, the G7 Working Group on Stablecoins released a report on *Investigating the Impact of Global Stablecoins*. Payments are in a state of flux, and innovation is extensive. Domestic payments, in most instances, are increasingly convenient, instantaneous and available 24/7. Yet, despite significant improvements in recent years, current payment systems still have two major failings: lack of universal access to financial services for a large share of the world's population and inefficient cross-border retail payments. Stablecoins, which have many of the features of earlier cryptocurrencies but seek to stabilise the price of the "coin" by linking its value to that of a pool of assets, have the potential to contribute to the development of more efficient global payment arrangements. This report lays out initial recommendations for both private sector stablecoin developers and public sector authorities to address the challenges and risks.

FSB: note on regulatory issues of stablecoins

On 18 October 2019, the FSB published an *Issues Note on Regulatory Issues of Stablecoins*. The paper responds to the G20 Leaders' Osaka Declaration, which noted the importance of monitoring developments in crypto-assets and remaining vigilant to existing and emerging risks, and asked the FSB and other standard-setting bodies to advise on additional multilateral responses as needed. The launch of stablecoin-type arrangements for domestic and cross-border retail payments with the potential to reach global scale could alter the current assessment that crypto-assets do not pose a material risk to financial stability. At the same time, the emergence of global stablecoins that could be used for cross-border payments and remittances by a large number of users in different countries could provide benefits to the financial system and the broader economy. In order to implement the G20 mandate and, building on earlier work by the G7, the FSB will submit a consultative report to G20 Finance Ministers and Central Bank Governors in April 2020, and a final report in July 2020.

BIS: the suptech generations

On 17 October 2019, the BIS' Financial Stability Institute published a report on *The Suptech Generations*. Financial authorities' use of technology has evolved over the years, leading to different generations of technology that culminate in what the paper considers as suptech. Suptech refers to the application of big data or artificial intelligence (AI) to tools used by financial authorities. There are many ways of exploring suptech tools and these are not mutually exclusive. They range from developing explicit suptech roadmaps, incorporating suptech into institution-wide digital transformation or data-driven innovation programmes, to establishing innovation labs or one-off programmes such as accelerators or tech sprints. While suptech is still in its infancy, it is gaining traction, with a significant number of suptech use cases found in the areas of misconduct analysis, reporting and data management. But most of these use cases are still experimental in nature.

BIS: innovation hub centre in Switzerland

On 8 October 2019, the SNB and the BIS signed an operational agreement on the BIS Innovation Hub Centre in Switzerland. [...] The Swiss Centre will initially conduct research on two projects. The first of these will examine the integration of digital central bank money into a distributed ledger technology infrastructure. This new form of digital central bank money would be aimed at facilitating the settlement of tokenised assets between financial institutions. Tokens are digital assets that can be transferred from one party to another. The project will be carried out as part of a collaboration between the SNB and the SIX Group in the form of a proof of concept. The second project will address the rise in requirements placed on central banks to be able to effectively track and monitor fast-paced electronic markets.

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DLT-related legislation and regulatory frameworks

Introduction

There have been a growing number of use cases of distributed ledger technology (DLT) in the international bond markets over the last three years.[1] While the majority of transactions have been of experimental nature, legal and regulatory uncertainty around the treatment of DLT appears to be one of the key challenges to its broader adoption.[2] There is a consensus that regulation is generally designed to be technology neutral. However, regulators and legislators have adopted different approaches to provide greater clarity and accommodate the use of DLT in the financial sector.

This article seeks to provide a non-exhaustive overview of recent DLT regulatory guidance, legislative initiatives, as well as related strategy papers and publications in selected jurisdictions across Europe, North America, and Asia-Pacific. Its aim is to provide a sense of the direction of travel, anticipating future regulatory DLT guidance and legislative change, which will pave the way for broader adoption of DLT. While the intention is not to cover regulatory approaches to crypto assets, relevant guidance and developments are considered insofar as they relate to the underlying technology.

This complements ICMA's Distributed Ledger Technology (DLT) Regulatory Directory (December 2019) as well as ICMA's previous publications on *Regulatory Approaches to FinTech and Innovation in Capital Markets* (September 2018) and *FinTech, DLT, and Regulation* (April 2017).

Overview

Adoption of new technologies comes with specific risks and uncertainties. Key areas addressed by DLT legislation, regulation, and guidance across multiple jurisdictions fall within the below categories:

- *Legal status:* Legal and regulatory interpretations have been addressed through legislative definitions of DLT and smart contracts, enhancement of digital securities investor rights, and in some jurisdictions the acknowledgement of technology-neutrality.
- *Interoperability and standardised protocols:* International standard-setting bodies are focused on the risk of fragmentation through promotion of industry consultation and technical paper releases.
- *Security/resilience and corporate governance*: Multiple jurisdictions have adopted guiding business principles as foundations for their DLT regulatory frameworks. Licensing and registration frameworks have also mitigated these business risks operating on DLT.

> **Multiple jurisdictions are taking initiatives in providing clarity to the market with legal definitions and specific requirements for DLT operations.**

Legislation and regulatory frameworks

Multiple jurisdictions are taking initiatives in providing clarity to the market with legal definitions and specific requirements for DLT operations.

1. Over 30 initiatives including proof-of-concepts and live transactions have been observed in the last three years as referenced by ICMA.

2. In addition to technical (eg scalability), operational (eg interoperability) and governance-related challenges of DLT networks.

Europe: For instance, France's Decree No. 2018-1226 of 24 December 2018 provided provisions for its previous Ordinance no. 2017-1674 of 8 December 2017, allowing for DLT representation and transfer of ownership of financial securities. This builds on the initial Ordinance no. 2016-520 of 28 April 2016 allowing short-term note "mini-bond" issuance on DLT. Law no. 2019-486 "Loi PACTE" of 22 May 2019 also introduces a special regulatory status for certain Digital Asset Service Providers and licensing requirements for non-financial digital asset custodian services.[3]

Italy's Law No. 12/2019 of 11 February 2019 with Decree Law No. 135, (Decreto Semplificazioni) of 14 December 2018 defined DLT and smart contracts, recognised legal effects of electronic timestamps and also electronic storage of documents on DLT.[4] Implementing technical standards are expected to be published by the Digital Italy Agency (AgID) in the coming months.

Other jurisdictions have developed standalone DLT regulatory frameworks to further innovation hubs and protect investors. Gibraltar's, Financial Services (Distributed Ledger technology Providers) Regulations 2017 (LN.2017/204), commenced on 1 January 2018, sets out nine guiding principles for DLT business conduct in addition to setting definitions, licensing and registration requirements. Gibraltar's Financial Services Commission (GFSC) also provides an overview of its DLT framework on a dedicated web page.

North America: In the United States, over 28 DLT-related resolutions and bills have been enacted or adopted at the State jurisdiction level. Notable Bills are Arizona's H.B. 2417 (signed by Governor March 2017), H.B. 2602 (signed by Governor April 2018), Illinois' H.B. 5553 creation of Blockchain Technology Act (Passed House April 2018) and Maryland's S.B. 136 (effective 1 October 2019) providing DLT/Blockchain definitions and legal status of smart contracts. A comprehensive list of Blockchain State Legislation is maintained by the NCSL.[5]

Asia: The Cyberspace Administration of China (CAC) released its Regulations on the Management of Blockchain Information Services which came into effect 15 February 2019. Key components include registration of individual and business users of blockchain services (real-names), periodic safety/security inspections of the services and a security assessments requirement to be undertaken for each new product and function of the service.[6] The first list of 197 blockchain-based services reviewed and filed by the CAC was publicly released 30 March 2019.

Recent publications and guidance on DLT

Over the last two years, international regulators have published a number of research papers and assessments in relation to DLT, while international standard-setting bodies have published DLT-specific standards. At national level, regulators have provided guidance, notably in jurisdictions where amendments to the regulatory framework are not envisaged or are being considered.

Global: From a global perspective, the FSB released its *Decentralised Financial Technologies – Report on Financial Stability, Regulatory and Governance Implications* (June 2019) and the International Standards Organisation (ISO) published its first Blockchain/DLT standards *ISO/TR 23455:2019* (September 2019) as part of their *Strategic Business Plan ISO/TC 307*.

Europe: The ECB FinTech Task Force published its *Potential Use Cases for Innovative Technologies in Securities Post-Trading Report* (January 2019). The European Commission's Expert Group on Regulatory Obstacles to Financial Innovation (ROFIEG) published its *30 Recommendations on Regulation, Innovation and Finance* (December 2019).

National: BaFin released its *Perspectives Issue 1. Digitalisation* (August 2018) and *Tokenisation* publication (May 2019). The German Federal Government also published its *Blockchain Strategy* paper (September 2019) following an earlier consultation *Key Issues Paper on Regulatory Treatment of Electronic Securities and Crypto Tokens* (March 2019).

FCA has previously released guidance through FS17/4: distributed ledger technology feedback statement (December 2017) and most recently the UK Jurisdiction Taskforce published its *Legal Statement on Crypto-Assets*

3. The Law Reviews, September 2019. The Virtual Currency Regulation Review - Edition 2 France.

4. Hogan Lovells, 15 February 2019. Italy recognises the legal value of DLTs and smart contracts

5. NCSL, Blockchain State Legislation, last updated 28 March 2019

6. Norton Rose Fulbright, February 2019. China issues new regulation on blockchain

Several further consultation and study papers on DLT are expected early in 2020, while several national authorities have released policy guidelines regarding the future direction of DLT regulation.

and Smart Contracts (November 2019) after public consultation (May 2019) on the current legal status and uncertainty of crypto-assets, DLT and smart contracts.

Other authorities are maintaining DLT information and guidance on dedicated webpages such as MAS's Blockchain/DLT page and ASIC's Information Sheet 219 (INFO 219).

What's on the horizon?

Several further consultation and study papers on DLT are expected early 2020, while several national authorities have released policy guidelines regarding the future direction of DLT regulation. The German Government's *Blockchain Strategy* adopted in September 2019 outlines its policy framework plan to reform German securities law to facilitate electronic bonds and the Swiss Federal Council has proposed amendments to allow for electronic registration of rights and increase legal certainty of DLT-lased assets among other objectives.

At the EU level, ESMA Chair Steven Maijoor in a keynote speech stated that ESMA "will continue to monitor markets closely to see whether firms are able to meet these [security, privacy and interoperability] challenges, enabling them to deliver DLT applications in securities markets at scale"[7] (February 2019), while the new European Commission's political guidelines proposed joint standard setting for new technologies, including blockchain.

Conclusion

Legal and regulatory uncertainty surrounding DLT remains a key challenge for wider adoption of the technology. However, it is evident that multiple authorities have taken proactive steps in providing clarity to capital markets. This has ranged from publishing guidelines such as the UK's FCA FS17/4, to introducing specific DLT legislation such as Italy' Law No. 12/2019, to adopting complete DLT regulatory frameworks as seen in Gibraltar.

Future regulatory changes for DLT have been indicated in recent publications such as Germany's *Blockchain Strategy* and Switzerland's *Federal Council Report to Improve Framework Conditions for DLT*.

We expect to see further standard setting and practical recommendations for DLT from international organisations with projects such as ISO/TC 307. In the shorter term, it can be expected that the implementation of proposed DLT legislative changes and the emergence of further definitions, requirements and guidance from a national perspective will pave the way for broader adoption of DLT in capital markets.

The full brief and DLT Regulatory Directory can be found on ICMA's website.

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7. Keynote speech by Steven Maijoor (Chair), ESMA 26 February 2019, Crypto-Assets: time to deliver. 3rd Annual FinTech Conference–FinTech and Regulation, p7

ICMA Capital Market Research

MiFID II/R and the Bond Markets: The Second Year
Published: 20 December 2019
Author: Gabriel Callsen, ICMA

ICMA Impact Study: Mandatory Buy-ins under CSDR and the European Bond Markets
Published: 27 November 2019
Author: Andy Hill, ICMA

ICMA Briefing: The Importance of Integrated Capital Markets and CMU
Published: 29 July 2019
Author: David Hiscock, ICMA

A Comparative Review of Practices and Procedures in the Russian and International Primary Debt Capital Markets
Published: 5 June 2019
Authors: ICMA/NFA Joint Report

ICMA ERCC Briefing Note: The European Repo Market at 2018 Year-end
Published: 15 January 2019
Author: Andy Hill, ICMA

ICMA AMIC/EFAMA Report on Liquidity Stress Tests in Investment Funds 2019
Published: 8 January 2019
Authors: ICMA/EFAMA Joint Report

The GFMA and ICMA Repo Market Study: Post-Crisis Reforms and the Evolution of the Repo and Broader SFT Markets
Published: 17 December 2018
Authors: ICMA/GFMA Joint Report

MiFID II/R and the Bond Markets: The First Year
Published: 6 December 2018
Editor: Andy Hill, ICMA

Adopting International Practices of Bond Trustee Arrangements in China
Published: 5 December 2018
Authors: ICMA/NAFMII joint publication

ICMA Discussion Paper: CSDR mandatory buy-ins and securities financing transactions
Published: 3 October 2018
Author: Andy Hill, ICMA

ICMA Briefing: Regulatory approaches to FinTech and innovation in capital markets
Published: 7 September 2018
Author: Gabriel Callsen, ICMA

The Asia-Pacific Cross-Border Corporate Bond Secondary Market: A report on the state and evolution of the market
Published: 30 August 2018
Authors: Andy Hill and Mushtaq Kapasi, both ICMA

How to Survive in a Mandatory Buy-in World
Published: 26 June 2018
Author: Andy Hill, ICMA

The European Corporate Single Name Credit Default Swap Market: A Study into the State and Evolution of the European Corporate SN-CDS Market
Published: 15 February 2018
Authors: Andy Hill and Gabriel Callsen, both ICMA

ICMA ERCC Briefing Note: The European Repo Market at 2017 Year-End
Published: 15 January 2018
Author: Andy Hill, ICMA

The Panda Bond Market and Perspectives of Foreign Issuers
Published: 19 October 2017
Authors: ICMA/NAFMII Joint Report

Market Electronification and FinTech
Published: 3 October 2017
Author: Gabriel Callsen, ICMA

Use of Leverage in Investment Funds in Europe
Published: 19 July 2017
Authors: AMIC/EFAMA Joint Paper

European infrastructure finance: a Stock-Take
Published: 13 July 2017
Authors: ICMA/AFME Joint Paper

The European Credit Repo Market: The Cornerstone of Corporate Bond Market Liquidity
Published: 22 June 2017
Author: Andy Hill, ICMA

Diary 2020

ICMA Workshops

DATE	ICMA Workshops
04 February *Register*	**Bond syndication practices for compliance and middle office professionals, London, 4 February** This workshop aims to give compliance professionals an in-depth and thorough understanding of the practices that are involved in launching a deal in the international debt capital market.
05 February *Register*	**Repo & the European repo market, London, 5 February** One day intensive training for those requiring a detailed familiarisation with repo and the repo market. Suitable for staff from all departments of a repo market participant and those supporting market participants with services such as legal advice and technology.
11-13 February *Register*	**Repo and securities lending under the GMRA and GMSLA, London, 11-13 February** 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. These two separate agreements are the essential underpinnings of the cross-border repo and securities lending markets.
London *22 January* **Frankfurt** *18 February*	**SFTR: repo reporting in practice** Ahead of the 2020 implementation ICMA is offering a one-day workshop on the practical aspects of reporting of repo transactions which will be required under the EU Securities Financing Transactions Regulation (SFTR).
London *25-26 February* **Melbourne** *3 March* **Sydney** *4 March*	**Introduction to green bonds** Introduces the underlying market drivers, the evolving regulatory framework and the main features of the green bond product and market based on the Green Bond Principles (GBP).

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Diary 2020

DATE	ICMA Conferences
29 January *Register*	**ICMA and Swiss Sustainable Finance joint conference: Developments in the green bond markets – the Swiss perspective, Zurich, 29 January 2020** In Switzerland, the momentum behind green bonds is beginning to build. This conference, jointly organised by ICMA and Swiss Sustainable Finance, is an opportunity to hear about regional developments with major Swiss issuers and investors describing the advantages of this form of finance.
13 March *Register*	**India Securities Summit, London, 13 March** Leading practitioners from banks, asset managers, law firms and corporates will discuss developments in debt capital markets in India and to review the key trends and opportunities at this conference organised jointly with DLS Piper and the London Stock Exchange.
19 March *Register*	**European Repo and Collateral Council AGM, London, 19 March** The ERCC's General Meetings provide a good opportunity to meet others in the market and hear about various current issues, including recent regulatory developments impacting the European repo market as well as the industry's latest best practice initiatives.
30 January *Register*	**11èmes Rencontres des Professionnels des Marchés de la Dette et du Change: "Les Defis de la Decennie", Paris, 30 January**
20 February *Register*	**HKMA and ICMA 2020 Sustainable Finance Conference, Hong Kong, 20 February** The Hong Kong Monetary Authority and ICMA will co-host a one day conference on sustainable finance, bringing together representatives from the official sector and the finance industry to discuss developments in this fast growing and high profile market.
04 March *Register*	**Secondary Markets Forum, Amsterdam, 4 March** Experts from the European fixed income market, representing banks and broker-dealers, investors and asset managers, as well as trading venues and technology providers will discuss the critical issues facing the European bond markets and the key drivers of evolving market structure and dynamics.

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ICMA Women's Network event
Madrid, 11 February

ICMA/Covered Bond Report conference
Frankfurt, 13th May

ICMA Future Leaders
Career Progression, Education, Networking.

La révolution digitale dans le secteur bancaire
Paris, 5 February

How to thrive in your capital market career
Hong Kong, 28 February
Frankfurt, 3 March

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- London, 2-3 April

Operations Certificate Programme (OCP)
- Luxembourg, 23-27 March

Collateral Management
- London, 30-31 March

SFTR – Repo reporting in practice
- London, 22 January

Repo and securities lending under the GMRA and GMSLA
- London, 11-13 February

Introduction to Green Bonds
- London, 25-26 February

Introduction to Green Bonds
- Melbourne, 3 March

Introduction to Green Bonds
- Sydney, 4 March

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GLOSSARY

ABCP	Asset-Backed Commercial Paper
ABS	Asset-Backed Securities
ADB	Asian Development Bank
AFME	Association for Financial Markets in Europe
AI	Artificial Intelligence
AIFMD	Alternative Investment Fund Managers Directive
AMF	Autorité des marchés financiers
AMIC	ICMA Asset Management and Investors Council
AMI-SeCo	Advisory Group on Market Infrastructure for Securities and Collateral
APA	Approved publication arrangements
APP	ECB Asset Purchase Programme
ASEAN	Association of Southeast Asian Nations
AUM	Assets under management
BCBS	Basel Committee on Banking Supervision
BIS	Bank for International Settlements
BMCG	ECB Bond Market Contact Group
BMR	EU Benchmarks Regulation
bp	Basis points
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
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
DCM	Debt Capital Markets
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
EDDI	European Distribution of Debt Instruments
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
ESAs	European Supervisory Authorities
ESCB	European System of Central Banks
ESFS	European System of Financial Supervision
ESG	Environmental, social and governance
ESM	European Stability Mechanism
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
ETF	Exchange-traded fund
ETP	Electronic trading platform
EU27	European Union minus the UK
ESTER	Euro Short-Term Rate
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 Markets Standards Board
FPC	UK Financial Policy Committee
FRN	Floating-rate note
FRTB	Fundamental Review of the Trading Book
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
GFMA	Global Financial Markets Association
GHOS	Group of Central Bank Governors and Heads of Supervision
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
HQLA	High Quality Liquid Assets
HY	High yield
IAIS	International Association of Insurance Supervisors
IASB	International Accounting Standards Board
IBA	ICE Benchmark Administration
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 fur 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
MAR	Market Abuse Regulation
MEP	Member of the European Parliament
MiFID	Markets in Financial Instruments Directive
MiFID II/R	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
NPL	Non-performing loan
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
PMPC	ICMA Primary Market Practices Committee
PRA	UK Prudential Regulation Authority
PRIIPs	Packaged Retail and Insurance-Based Investment Products
PSEs	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
RFRs	Near risk-free rates
RM	Regulated Market
RMB	Chinese renminbi
RPC	ICMA Regulatory Policy Committee
RSP	Retail structured products
RTS	Regulatory Technical Standards
RWA	Risk-weighted asset
SBBS	Sovereign bond-backed securities
SEC	US Securities and Exchange Commission
SFT	Securities financing transaction
SGP	Stability and Growth Pact
SI	Systematic Internaliser
SMEs	Small and medium-sized enterprises
SMPC	ICMA Secondary Market Practices Committee
SMSG	Securities and Markets Stakeholder Group (of ESMA)
SARON	Swiss Average Rate Overnight
SOFR	Secured Overnight Financing Rate
SONIA	Sterling Overnight Index Average
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
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
TONA	Tokyo Overnight Average rate
TRs	Trade repositories
UKLA	UK Listing Authority
VNAV	Variable net asset value

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