ICMA

International Capital Market Association

QUARTERLY REPORT

ASSESSMENT OF MARKET PRACTICE AND REGULATORY POLICY

INSIDE:

CAPITAL MARKETS UNION AND BREXIT

BENCHMARK REFORM AND THE FUTURE OF LIBOR

IMPLEMENTATION OF MIFID II/R

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ICMA

International Capital Market Association

ICMA promotes resilient and well-functioning international capital markets, which are necessary for economic growth. ICMA's market conventions and standards have been the pillars of the international debt market for nearly fifty years.

Membership continues to grow and we now have around 530 member firms in 63 countries.

Among the members are global investment banks, commercial and regional banks, brokers, private banks, institutional asset managers, pension funds, central banks, sovereign wealth funds and other institutions with a significant interest in the international capital market, such as supranational institutions, infrastructure providers, rating agencies and leading law firms.

ICMA members work with ICMA through its market practice and regulatory policy committees and councils to provide expert views on the issues affecting the international capital markets. The committees act as a forum for discussion and for reaching consensus on topics of common interest, developing recommendations for best market practice and the efficient operation of the markets and considering policy responses to regulators.

FEATURES:

01:

Capital Markets Union and Brexit

By Paul Richards

02:

Benchmark reform and the future of LIBOR

By Catherine Wade

03:

Implementation of MiFID II/R

All articles highlighted with

CONTENTS

4 FOREWORD

5 MESSAGE FROM THE CHIEF EXECUTIVE

6 QUARTERLY ASSESSMENT
6 Capital Markets Union and Brexit

15 INTERNATIONAL CAPITAL MARKET FEATURES
15 Benchmark reform and the future of LIBOR: implications for the primary bond markets
20 The state and evolution of the Asian cross-border corporate bond markets
23 Bond Connect: a new channel into China's onshore bond market
25 Market electronification and FinTech

27 INTERNATIONAL CAPITAL MARKET PRACTICE AND REGULATION
27 Summary of practical initiatives by ICMA

29 PRIMARY MARKETS
29 Omnibus III and prospectus approvals
30 EU Prospectus Regulation
30 M PRIIPs and MiFID II/R product governance
32 ICMA Corporate Issuer and Financial Issuer Forums
33 Asset-Backed Commercial Paper

34 SECONDARY MARKETS
34 M MiFID II/R FAQ: impact on non-EU/EEA secondary bond market participants
38 M MiFID II/R implementation: road tests and safety nets
40 M MiFID II/R implementation: ESMA guidance
41 The ECB's Corporate Sector Purchase Programme
42 The European single name CDS market
43 High-level data on corporate bond market activity in Europe
44 ICE Data Services Corporate Bond Market Liquidity Tracker

46 REPO AND COLLATERAL MARKETS
46 M European repo and collateral market developments
48 Autumn 2017 ICMA ERCC General Meeting
48 SFT Regulation
49 Results of pilot survey of repo markets in Asia-Pacific

50 ASSET MANAGEMENT
50 M MiFID II/R implementation: research unbundling
50 Leverage in investment funds
51 Fund liquidity risk management
51 Central Bank of Ireland: ETFs
52 AMIC Council
53 European infrastructure finance

54 GREEN, SOCIAL AND SUSTAINABLE BOND MARKETS
54 Green, social and sustainable bond market developments
56 IFFIm's impact on SRI reflected in new Social Bond Principles
57 IFC's social bonds: doing good and doing well through the bond markets

58 INTERNATIONAL REGULATORY DIGEST
58 G20 financial regulatory reforms
61 ICSA's contribution to global capital markets
62 European financial regulatory reforms
63 Financial benchmarks
64 Credit rating agencies
65 OTC (derivatives) regulatory developments
66 Market infrastructure
70 Macroprudential risk
73 FinTech and government bonds in Kenya

74 ICMA CAPITAL MARKET RESEARCH

75 ICMA EVENTS AND EDUCATION

79 GLOSSARY

M This symbol indicates articles referring to MiFID II/R

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Robust and resilient markets

By Martin Egan

Markets have functioned well for the majority of 2017 despite initial concerns of increased volatility, and I expect this situation to remain for the rest of the year. At the start of the year there were many concerns for market practitioners. Geopolitical risk was "front and centre" and undoubtedly remains a notable threat to market stability. However, concerns over impending regulation, market illiquidity, the US political background, protectionism, rising interest rates, ending of quantitative easing, the future of Europe ahead of an election year in the Netherlands, France and Germany, and of course Brexit, all resonated as stress points for the year ahead. In fact I can rarely remember a year starting with such concerns, at least since the international financial crisis.

Yet, here we are at the end of the third quarter and markets remain open and robust, providing opportunities for issuers, investors and underwriters alike. The resilience of the marketplace continues to be impressive. With central banks reducing financial support for the market gradually and interest rate rises coming more slowly than expected, one has to expect a constructive environment ahead. This has generated many bright spots, with borrowing costs remaining at historical lows fuelling economic growth while the search for yield will continue to gather impetus in an orderly fashion. So, all in all pretty positive. However, I want to elaborate on four key areas of focus that I highlighted as your new Chairman at the Luxembourg AGM on how ICMA can work with its membership to help prepare for what will be ground-breaking change in the months ahead.

Geopolitical risk remains a key concern for the marketplace and will remain a core driver of sentiment going ahead. Despite this, markets are functioning well and it is hard to remember a period this year when pronounced instability resulted in any notable form of market stress. We must remain vigilant, however, and attempt to keep markets functioning well at all times.

Green and social bonds: ICMA is actively involved in the development of the green and social bond market in its role as Secretariat of the Green and Social Bond Principles. Volumes this year already exceed last year's total. The success of the French Government's €7 billion 30 year OAT will be a precursor to further jumbo issuance ahead.

Technology: Credit and issuance markets have appeared slow to embrace technology and especially automation of processes, but this is clearly changing rapidly. In primary, credit, repo and collateral markets, ICMA is working with providers to improve offerings in a compliant and regulatory-focused environment. Direct investor access to order books and automation of the issuance process are some of the key areas with positive momentum.

Regulation: MIFID II/R will have far reaching effects for the European, but also the global, marketplace. Institutions are in various states of preparation for 3 January 2018, and the next few months will be critical. At this juncture much remains to be done, with regulatory clarity finally taking shape to give some sense of direction of travel. There is cause for concern as time is short but renewed focus on reporting, transparency and market integrity will be generally welcomed but also with risks linked to an overly bureaucratic process. ICMA's Market Practice, Legal and Documentation, and Regulatory Policy Committees are fully engaged to find solutions with market counterparts and regulators.

Away from the four main themes highlighted, we remain very focused on secondary market liquidity and fluidity of repo and collateral markets. We continue to develop activities in Asia and reinforce critical linkage of all relevant markets. In summary, we have healthy markets but face a maelstrom of regulatory change ahead. There is plenty to digest at a macro level, as well as Brexit. Altogether, ICMA's role has never been more relevant in bringing key market participants and regulators together to shape the market of the future in an efficient and constructive manner. It is imperative that all types of market counterpart have a seat at the table and are given forums to comment on how they want to progress. We must remember that there are many components and complexities in having well-functioning markets and every viewpoint has relevance. I know that the value attached by our membership to ICMA's involvement is pronounced. We must all work together to reach the best outcomes possible.

Martin Egan *is Global Co-Head of Primary and Credit Markets, Global Markets, BNP Paribas, and Chairman of ICMA.*

The deadline approaches

By Martin Scheck

With the 3 January 2018 deadline drawing inexorably closer, it is no surprise that the intensity of our focus on MiFID II/R related workstreams has increased. Our committees are striving to clarify the open points with members, law firms and regulators, to facilitate implementation of this swathe of new EU legislation. Since the last Quarterly Report, we have issued the first three monthly MiFID II/R briefings for members and will continue to publish these in the run-up to implementation, and we are also holding a series of MiFID II/R workshops in European financial centres.

MiFID II/R has significant extra-territorial impact. Outside the EU, the understanding of the impact is often much less developed and the readiness of members to comply with the provisions somewhat patchy. We have held workshops in Hong Kong and Singapore as well as providing FAQs for our members located outside the EU. We expect to hold more briefing calls and/or workshops for members in Asia.

We have significant concerns about the implications of MiFID/R in a number of areas and I will just comment on two of these.

(i) *Research unbundling*. Whilst the central tenet of investors unbundling research from execution services is worthy, the impact of the measures being discussed on the availability of research is unclear and may well differ depending on the type of institution and its size. For example, research provision for SMEs may decline, compromising their access to the capital markets at a reasonable cost. This would run directly counter to the stated objectives of CMU. More analysis leading to a better understanding of the potential consequences is needed.

(ii) The proposed *product governance* regime is likely to curtail further the appetite of issuers to engage with retail investors. Coupled with the Prospectus Regulation and PRIIPs, we can envisage a situation where retail investors will have significantly less access to high quality, simple, straight bond issues from many of the highest rated issuers in the world than they currently enjoy. Quite apart from the fact that again this runs counter to the objectives of CMU, it is also counter-intuitive when one considers that retail investors are able to buy shares in small amounts in the issuing companies but not their bonds.

This Quarterly Report contains more detail on our MiFID II/R related work. Our staff are always ready to answer questions directly, or via the Help Desk.

Many of you will be aware of the surge in discussions regarding the migration of LIBOR to a benchmark rate based on observed transactions following the speech by Andrew Bailey, Chief Executive of the UK Financial Conduct Authority, in July. Subsequently ESMA, the European Commission and the ECB announced a working group to consider the creation and adoption of a risk-free overnight rate as an alternative to current benchmarks used in the euro area. This raises many questions at all levels, ranging from what benchmark rate to use to how to ensure continuity of contract, what impact there will be on existing bonds having IBORs as reference rates and what the arrangements will be for new issues during the intervening period. This topic is of great interest to all our members: over 400 joined the call we held to discuss this. We will keep our members updated on progress.

Our secondary market work in Asia is expanding. We have extended our electronic trading mapping survey to include platforms used in the region, and are augmenting our liquidity research through interviews with Asian counterparties. Repo is a major topic for our Asian members. We regularly hold GMRA workshops in the region, and have published a pilot Asian Repo Survey report.

Cooperation with other associations is critically important. Following the successful report published in 2016 with EFAMA on liquidity risk in investment funds in Europe, we published in July a further joint study on the use of leverage in investment funds in Europe. Also in July we published jointly with AFME an update on infrastructure finance entitled *European Infrastructure Finance: a Stock-take*.

As a final note, all our work is set against a backdrop of increased potential capital market fragmentation because of heightened national and regional political tensions, including the current negotiations around Brexit. This creates risks to the EU's Capital Markets Union project and these are explored further in the following Quarterly Assessment.

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Capital Markets Union and Brexit

By Paul Richards

Summary

What are the prospects for EU Capital Markets Union and how will they be affected by Brexit? At one level, Brexit makes Capital Markets Union in the EU27 a more important initiative, as capital markets are less developed in the EU27 than in the UK. The prospects for Capital Markets Union in the EU27 would also benefit from renewed political momentum in the euro area to strengthen the economic pillar of Economic and Monetary Union. But at another level, Brexit divides Capital Markets Union into two between the EU27, on the one side, and the UK – as the largest international financial centre in the EU – on the other. There is a risk that the negotiations between the EU27 and the UK could lead to international capital market fragmentation and financial instability, to the disadvantage of both sides. This paper considers possible alternatives which would be in their mutual interest.

Introduction

1 The paper addresses three related questions:

- First, what are the prospects for making further progress in the EU towards Capital Markets Union?
- Second, how can the prospects for Capital Markets Union be improved by strengthening the economic pillar of Economic and Monetary Union?
- Third, how will the prospects for Capital Markets Union be affected by Brexit, and what can be done about this?

The European context

New prudential regulations have been introduced in response to the international financial crisis of 2007-2009 to improve bank resilience by increasing capital and liquidity requirements, though the process of bank recapitalisation has taken longer in the EU than the US; and new regulations also provide that, in the event that banks fail in future, selected creditors as well as shareholders should be bailed *in* rather than relying on taxpayers to bail them *out*. In addition, new conduct of business regulations have been introduced to improve market standards, backed by fines for mis-selling. These measures are all designed to rebuild and maintain public trust in the stability, safety, soundness and fairness of the financial system.

Following the sovereign debt crisis of 2010-2012 in several euro area countries, which led to the ECB's initiative in 2012 to do "whatever it takes" to save the euro, the ECB has introduced quantitative easing (QE), accompanied by negative short-term interest rates, to bring inflation in the euro area back towards its target of close to, but below, 2% per annum.

There is increasing evidence that, in response, the European economy is at last recovering on a sustainable basis, and that unemployment in the euro area is declining, though youth unemployment is still very high in some euro area countries. The economic recovery appears to be extending to those euro area countries whose governments had to be bailed out in response to the sovereign debt crisis of 2010-2012. But there are still questions about their long-term economic competitiveness with Germany.

Following the elections this year in France and Germany, there may be a new political opportunity for closer economic integration in the euro area, supported by the European Commission. The UK, by contrast, has voted to leave the EU and triggered Article 50 of the EU Treaty, leading to negotiations with the European Commission on behalf of the EU27 on the terms of UK withdrawal from the EU by 29 March 2019.

EU Capital Markets Union

2 The European Commission's initiative on Capital Markets Union (CMU) is designed to develop capital markets in the EU27 through greater capital market integration across national borders, with the objective of strengthening the EU economy and stimulating investment to create jobs. In developing EU capital markets, the Commission does not intend to replace bank financing, but to complement it. This is particularly important in the EU27, whose capital markets are not as developed as in the UK or the US. The CMU Mid-Term Review[1] has provided an opportunity to assess progress to date. There are five main ways in which to make further progress towards CMU in the medium term:

3 *New EU measures:* CMU involves the introduction of new EU measures by 2019 to develop and integrate capital markets across the EU.[2] Out of 33 measures originally envisaged as part of the CMU work programme, 20 had been introduced by the time of the Mid-Term Review. New measures planned but not yet fully implemented (eg measures relating to insolvency reform and taxation) could potentially make a significant difference to capital market integration across national borders in the EU, though agreement in the EU on measures which make the most significant difference have often proved politically the most intractable in the past.

4 *Review of existing measures:* CMU also involves ensuring that existing EU measures are fit for purpose. Review clauses in EU legislation provide an opportunity to check this. The Commission's Call for Evidence was designed to assess regulatory reforms introduced in response to the international financial crisis, without altering the broad thrust of the reforms. Respondents drew attention to the need for a number of regulatory improvements (eg to offset the potentially harmful effects of some specific regulatory calibrations on market liquidity),[3] and these improvements need to be implemented following the Mid-Term Review.

5 *Supervisory convergence:* The effectiveness of CMU depends on achieving greater supervisory convergence across the EU. This involves completing the Single EU Rulebook[4] and ensuring that new legislative measures are implemented and enforced across the EU in a consistent way.[5] Following the CMU Mid-Term Review, the European Commission has proposed greater powers for the European Securities and Markets Authority (ESMA) to ensure supervisory harmonisation across the EU27.[6] ESMA already has direct responsibility for supervising credit rating agencies and trade repositories, and the Commission proposed in June that ESMA should take direct responsibility for the oversight of central counterparties, in close consultation with the ECB. By 2019, the Commission envisages that the first steps may also be taken towards establishing a single EU capital markets supervisor.[7]

6 *Financial stability:* CMU is intended to increase financial stability in the EU by diversifying funding channels and sharing risks across national borders to make the EU financial system more resilient, recognising that international capital flows are now only half their pre-crisis levels in relation to world output.[8] In a Monetary Union such as the euro area, risk sharing across national borders through the capital markets is particularly important because a single monetary policy is not able to address asymmetric shocks, which affect some countries more than others. Risk sharing can also help to offset the potential threat to financial stability arising from financial integration. Without risk sharing, financial stability may be vulnerable to cross-border contagion.[9]

1. European Commission Communication: *Mid-Term Review of the Capital Markets Union Action Plan*, 8 June 2017.

2. The objectives of the measures are summarised by the European Commission as to: "strengthen the capacity of EU capital markets; encourage finance for innovation, start-ups and non-listed companies; make it easier for companies to raise capital on public markets; invest for the long term in infrastructure and sustainable investments; foster retail investment; strengthen banking capacity to support the wider economy; and facilitate cross-border investment": *Mid-Term Review of the Capital Markets Union Action Plan,* 8 June 2017.

3. See, for example, the ICMA response to the European Commission consultation on the Capital Markets Union Mid-Term Review, 10 March 2017.

4. See: Danièle Nouy, Chair of the Supervisory Board of the ECB: "In Europe, we have 19 versions of the Single Rulebook, and each one is slightly different from the others. Such a fragmented set of rules is a problem. It increases risks, and it makes European banking supervision more complex and costly for banks.": *Regulation and Supervision in Europe – Can Many Cooks Make a Good Broth?* Frankfurt, 15 May 2017.

5. This will be easier if the EU makes greater use of Regulations, which apply directly in EU Member States, rather than Directives, which have to be transposed by EU Member States into national law.

6. European Commission Communication, *Reinforcing Integrated Supervision to Strengthen CMU and Financial Integration in a Changing Environment,* 20 September 2017.

7. European Commission: *Reflection Paper on the Deepening of EMU:* 31 May 2017.

8. ECB: *The Future of Globalisation*, November 2016.

9. See: Vitor Constancio, Vice-President of the ECB: *Risk Sharing and Macroprudential Policy in an Ambitious Capital Markets Union,* Frankfurt, 25 April 2016.

7 *Market infrastructure:* In parallel with the Commission's work on CMU, the ECB has made considerable progress in developing and integrating the financial market infrastructure for the euro through the TARGET2 payment system and the TARGET2-Securities settlement system linking national and international Central Securities Depositories. The ECB now has plans: to consolidate TARGET2 and TARGET2-Securities; to provide settlement services to support instant payments; and to establish a potential Eurosystem collateral management system.[10] Even so, there are still many barriers to post-trade services across financial markets which remain to be addressed. The European Post-Trade Forum's recent report on these barriers has provided the basis for a Commission consultation, which will inform a Communication on post-trade, planned for the end of 2017.[11]

CMU and euro area integration

8 The prospects for EU capital market integration through CMU would be improved if accompanied by policy changes to strengthen the economic pillar of Economic and Monetary Union in the euro area. Following the elections this year in France and Germany, there may be a new political opportunity for closer economic integration in the euro area, and a proposal has been put forward by the President of the European Commission, though the response in Germany is not yet clear and the question of the secession of Catalonia from Spain has arisen again.[12] Economic and Monetary Union still represents a "half-way house", in which there is a fully developed Monetary Union, with the ECB taking responsibility for monetary policy in the euro area, but not a fully developed Economic Union, where responsibilities remain largely at national level.[13] Strengthening the economic pillar will require closer economic convergence within the euro area; agreement on a path to fiscal integration; and a settlement between the euro area and other EU countries, which will still represent 15% of EU GDP after Brexit.[14] But it will also depend on resolving two specific issues which are closely related to CMU: the completion of Banking Union; and the search for a European safe asset as a euro area benchmark.

(i) Banking Union

9 Progress has been made towards Banking Union, which is intended both to increase the resilience and integration of the euro area banking system and, by doing so, to support the integration of capital markets in the EU.[15] Banking Union and Capital Markets Union are seen as complementary parts of a complete Financial Union. But in the case of Banking Union, it is important to distinguish between three separate steps. More progress has so far been made on some steps than others:

10 First, the ECB has taken direct responsibility for supervising 130 key banks in the euro area through the *Single Supervisory Mechanism*. This should help to improve bank resilience by ensuring that there is a fully consistent approach to bank supervision across the euro area, including on stress testing; and that the interdependence between some banks and their national governments through bank holdings of government debt, and the overhang of non-performing bank loans, are both reduced to more manageable levels, particularly if supported by a sustained economic recovery in the euro area.

11 Second, the *Single Resolution Board* has been established to ensure that failing banks are resolved without recourse to the taxpayer. Under the Bank Recovery and Resolution Directive (BRRD), bank resolution is to be financed by banks' shareholders and selected creditors, and by a Single Resolution Fund, pre-financed by the banking industry. But if this is not sufficient, a credible fiscal backstop to the Single Resolution Fund is still needed (eg through a credit line to the Single Resolution Fund from the European Stability Mechanism).[16] The new arrangements for bank recovery and resolution have been put to the test this year. In Spain, Banco Popular was sold in June to Banco Santander for €1 after equity and junior debt holders

10. Yves Mersch, Member of the ECB's Executive Board: September 2016.

11. European Commission: *Post-trade in a CMU: Dismantling Barriers and Strategy for the Future: Consultation Document,* 23 August 2017. The main barriers identified by the European Post-Trade Forum, and subject to consultation, include: diverging corporate action processes; lack of convergence and harmonisation in information messaging standards; lack of harmonisation and standardisation of ETF processes; complexity of post-trade reporting; unresolved issues on reference data and standardised identifiers; legal uncertainty about risk mitigation techniques; deficiencies in the protection of client assets; inadequate EU rules on finality; lack of harmonisation of registration and investor identification rules; and inefficient withholding tax procedures.

12. See: Jean-Claude Juncker, European Commission President: State of the Union Address, 13 September 2017.

13. See: European Commission: *Reflection Paper on the Deepening of EMU:* 31 May 2017; and *The Five Presidents' Report:* June 2015.

14. The settlement negotiated by the British Government with the EU27 in February 2016 failed when the UK voted to leave the EU in the Referendum in June 2016. There is a case for reviving the settlement to protect the position of EU countries still in the EU outside the euro area.

15. See: Vitor Constancio, Vice-President of the ECB: *Synergies Between Banking Union and Capital Markets Union,* Brussels, 19 May 2017.

16. European Commission: *Reflection Paper on the Deepening of EMU:* 31 May 2017 (page 20).

were bailed in without a cost to the Spanish taxpayer. But in Italy, Banca Monte di Paschi di Siena was recapitalised and restructured, and the regional banks of Vicenza and the Veneto were bailed out by the Italian Government in June and sold to Banca Intesa Sanpaolo, following a decision to exempt them from the BRRD. The head of the Single Resolution Board has since proposed that this potential loophole should be reviewed.

12 The third issue, which remains to be resolved, is the need to reach agreement on a *European Deposit Insurance Scheme* to insure deposits with banks up to €100,000 across the euro area in place of existing national schemes. Agreement has not so far been reached, mainly because of concern in Germany that German banks would be required to bail out insured depositors with banks in other euro area countries. But German resistance to common deposit insurance may become less pronounced if banking reform in the euro area is successful in ensuring that banks – especially in Italy and Spain – are more resilient.

(ii) A European safe asset

13 The issuance of government debt in the euro area remains largely a national responsibility.[17] German Bunds are treated in the market as the "safest" national asset (eg when there is a flight to safety in financial markets). Various options have been considered for creating a European safe asset (ie a "eurobond") which would be intended to act as a benchmark for the euro area equivalent to Treasuries in the US, provided that there is sufficient political and economic integration in the euro area to ensure that the euro project itself is considered "safe". There are two main options currently under consideration:

14 One option would be for euro area governments to provide *joint and several guarantees* on new issuance of euro-denominated national government debt in the euro area. The provision of joint and several guarantees would result in a euro area benchmark which would reduce the cost of funding for those sovereign issuers in the euro area which currently have lower credit ratings, but might increase the cost of funding for those which currently have triple A ratings. In addition, there is a concern that the provision of joint and several guarantees would weaken financial discipline among the governments of less creditworthy euro area countries. More fundamentally, there would be political resistance, particularly in Germany, to the provision of taxpayer guarantees of this kind. Joint and several guarantees would also require a change in the EU Treaty.

15 The other option under consideration (eg by the European Systemic Risk Board) is for the issuance of euro-denominated *sovereign bond-backed securities* (SBBS), which would effectively carry several, but not joint, guarantees by sovereigns in the euro area. The pool of sovereign assets in the SBBS would be weighted (eg by GDP). SBBS would be designed to promote risk sharing and reduce the interdependence between banks and their own sovereigns. However, it is not clear to what extent SBBS would increase risk sharing in practice, as there is a high correlation between most euro area sovereign risks. Nor is it clear whether risk sharing would significantly increase the resilience of banks which buy SBBS (rather than buying the debt of their own sovereign) unless the pool of sovereign assets underlying the SBBS were split between a senior (ie "safe") and a junior (ie less "safe") tranche. This might make the junior tranche less liquid and more difficult to sell to junior investors without a significantly higher yield, leaving a much lower yield for senior investors. A major uncertainty is the regulatory treatment of SBBS: whether SBBS would be treated as securitised products or sovereign assets for regulatory purposes; and whether and, if so, how the current regulatory treatment of sovereign exposures (which are generally risk-free for capital purposes) will be changed. At present, given that sovereign debt in less creditworthy countries carries a relatively high yield and is generally treated as risk-free for capital purposes, there is little incentive for bank holders of the debt of their own sovereign to diversify. To demonstrate the authorities' commitment to SBBS, a public sector issuer might need to test the market first, and possibly also provide liquidity in the secondary market.[18]

CMU and Brexit

16 Brexit will make Capital Markets Union in the EU27 a more important initiative, as capital markets are less developed in the EU27 than in the UK. But the immediate impact of Brexit will be to reduce the scope of CMU, given the size of London as a European as well as a global financial centre, even if there is a transfer of business in response to Brexit from London to financial centres in the EU27. Costs for end-users of capital markets will also increase as a result of Brexit, if capital market firms have to operate in two centres rather than one. While it may become easier and quicker for the EU27 to reach decisions on capital markets regulation without the UK, the market-

17. However, the European Investment Bank and the European Stability Mechanism, among others, borrow at European level. It is also important to note that there are already very substantial claims by creditor countries on debtor countries in the euro area which have been accumulated through the TARGET2 payment mechanism.

18. The issuance of euro bills has also been suggested as a pilot project.

friendly influence of the UK on decision-making at EU level will be lost, though the UK will still influence decision-making at global level.

17 CMU is designed to encourage capital market integration across national borders in the EU, and capital market integration could potentially also benefit from closer economic integration in the euro area. The question posed by Brexit is whether capital market integration is solely of benefit to the EU27 across national borders *internally* in the EU27, or whether open and competitive markets would benefit the EU27 *internationally* as well. Clearly, it is important that promoting international capital market integration should be consistent with ensuring financial stability, which is in the EU's public interest. In order to assess these issues, this section is divided into three: capital market preparations for Brexit; capital market operations after Brexit; and capital market regulation after Brexit. The conclusion is that a sensible agreement between the EU27 and the UK on the terms of Brexit is in their mutual interest.

(i) Capital market preparations for Brexit

18 Following the UK Referendum on 23 June 2016, the British Government proposed that the UK should leave the EU Single Market when it leaves the EU by 29 March 2019, and instead negotiate – as a third country – a new free trade agreement with the EU27.[19] There is still considerable uncertainty in international capital markets about the prospective outcome of the negotiations between the UK and the EU27. Two key issues affecting international capital markets relate to the need for sufficient time to prepare for changes resulting from Brexit, and the need for legal certainty when Brexit takes place:

19 *Time to prepare:* A free trade agreement is very unlikely to be reached before the UK leaves the EU because the length of time likely to be needed to negotiate a free trade agreement is much greater than the length of time until Article 50 expires, and because the European Commission insists that only the framework of an agreement can be negotiated before Article 50 expires, while a detailed free trade agreement can only be negotiated afterwards and will take time to ratify. Capital market firms will need long lead-times to prepare for Brexit, and have already drawn up contingency plans to ensure that they can continue to serve all their clients without disruption.[20] The outcome of the Brexit negotiations will be uncertain until a late stage, as "nothing is agreed until everything is agreed". Consequently, a transition period[21] between the UK and the EU27 will need to be agreed before Brexit to cover the period after Brexit (until a free trade agreement comes into effect) in order to avoid the risk of a regulatory "cliff edge". There would be a "cliff edge" if the UK were to leave the EU either with no withdrawal agreement at all or an agreement involving substantial regulatory change at the outset. This would be disruptive to capital markets and risk damaging financial stability on both sides.[22]

20 Agreement between the UK and the EU27 on a transition period needs to be reached as early as possible during the Article 50 negotiations, and publicly announced (even if the announcement is subject to finalisation of the withdrawal agreement later), to avoid market uncertainty. Capital market firms will also want to be confident that regulatory changes will be made only once (ie at the end of the transition period) and not twice (at both the beginning and the end), and that they have a clear idea of the changes planned.[23] If that is not possible, given the long lead-times, capital market firms will need to implement their contingency plans on the grounds that they may not be able to rely on a transition period after Brexit. Some have already started to do so.

21 In Florence on 22 September, the British Prime Minister proposed such a period of "implementation" (ie transition) during which "access to one another's markets should continue on current terms" for a "strictly time-limited period" of "around two years", and under which the framework "would be the existing structure of EU rules and

19. This is because the British Government's objectives on Brexit involve taking back control of the UK's borders by limiting EU immigration to the UK, and taking back control of UK laws by bringing an end in the UK to the direct jurisdiction of the European Court of Justice. These objectives are not consistent with remaining in the EU Single Market when the UK leaves the EU.

20. In addition to preparing for Brexit, banks with headquarters outside the EU have been required since 2016 to set up a holding company for their EU subsidiaries; and in the UK banks are preparing to ring-fence their retail from their investment banking activities in separate entities by January 2019.

21. A transition period is described by the British Government as an "implementation period" or an "interim period".

22. See Andrew Bailey, Chief Executive of the FCA: "We need to preserve close regulatory and supervisory links with the EU. Looking ahead, strong coordination is a sensible approach to take in order to demonstrate the strength of the system. I would point to four permanent features: comparability of rules, but not exact mirroring; supervisory coordination; exchange of information; and a mechanism to deal with differences. I would add to this importance of transitional arrangements being put in place which allow for a smooth path to the new post-Brexit world.": *Why Free Trade and Open Markets in Financial Services Matter:* Reuters Newsmaker, London, 6 July 2017.

23. On 27 August, the Opposition spokesman for Exiting the EU stated that Labour's policy would be to stay in the EU Single Market and Customs Union during the transition period after the UK leaves the EU.

regulations", so that businesses "should only have to plan for one set of changes in the relationship between the UK and the EU". The detailed arrangements for this implementation period would need to be agreed "as early as possible". However, the Prime Minister recognised that "the EU Institutions will need to adopt a formal position" on the UK's proposal.[24]

22 *Legal certainty:* In order to avoid legal uncertainty over Brexit, the British Government has accepted that EU law will continue to apply in the UK until the UK leaves the EU; and has introduced into Parliament the Repeal Bill to take EU law into UK law when Brexit takes place.[25]

- In the *narrow* sense in which contractual provisions may be invalidated or disrupted, these measures may not in themselves avoid legal uncertainty with respect to jurisdiction and choice-of-court clauses in cross-border financial contracts outstanding when Brexit takes place, and for new cross-border financial contracts entered into after Brexit. Recognition of the governing law, including contracts governed by English law, should not alter, with the EU courts continuing to give effect to non-EU law under Rome I. The position is less clear in relation to jurisdiction. The Brussels I Regulation, which provides for recognition and enforcement of judgements between EU Member States, will cease to apply to the UK after Brexit. It is not yet clear which measures will be taken to support jurisdiction enforcement: possibilities include a revival of pre-Brussels Convention bilateral treaties, adherence to the Lugano Convention and ratification of The Hague Convention.
- In the *broader* sense of contractual uncertainty arising from the risk that capital market firms may no longer all be authorised to operate across the EU27 if passporting ends when Brexit takes place, the UK and EU27 authorities need to reassure market participants that the continuity of their cross-border financial contracts will not be affected by Brexit. One way of providing such reassurance would be for the UK and the EU27 authorities jointly to announce as soon as possible that cross-border financial contracts between market participants in the UK and the EU27 outstanding when Brexit takes place would be "grandfathered", for example by providing for this in the UK/EU27 withdrawal agreement.[26] An alternative would be for legislation to be introduced in both the UK and the EU27 to protect the long-term validity of existing contracts.[27] The objective would be similar to the provisions for continuity and freedom of contract in the Regulation under Article 235 of the Treaty (EC/1103/97) in all EU Member States, including the UK, when the euro was introduced in 1999.[28]

(ii) Capital market operations after Brexit

23 It is in the interests of both the UK and the EU27 for capital market operations to continue after Brexit with the minimum of disruption. Subject to the outcome of the negotiations between the UK and the EU27, there appear to be two main options for capital market firms operating in both the UK and in the EU27:

24 *Mutual recognition of regulatory equivalence:* One option is to rely on mutual recognition of regulatory equivalence between the UK and the EU27, to the extent that this is practicable. At present, regulatory equivalence consists of a patchwork of equivalence, endorsement, recognition and third country passporting for some – but not all – EU capital market regulations. There are provisions for determining equivalence in some EU regulations but not others and, where equivalence does apply, it is not always complete; determining equivalence involves a judgment by the European Commission as well as a technical assessment, and takes time; and the determination of equivalence can be withdrawn at short notice, though this has not happened to date. It is also relevant to note that the assessment of regulatory equivalence is based on measuring outcomes, but that outcomes are not straightforward to measure. For an equivalence assessment in the case of the

[continued on page 13]

24. British Prime Minister, *A New Era of Cooperation and Partnership Between the UK and the EU,* Florence, 22 September 2017. During the implementation period, the Prime Minister said that "people will continue to be able to come and live and work in the UK", subject to a registration system; and that the UK's partners will not "need to pay more or receive less over the remainder of the current budget plan as a result of our decision to leave."

25. The British Government won a vote in the House of Commons on the EU (Withdrawal) Bill – ie the Repeal Bill – on 11 September 2017. But it is not yet clear whether, and if so how, the Repeal Bill will be amended during its remaining passage through Parliament.

26. See also: HM Government: *Providing a Cross-Border Civil Judicial Cooperation Framework:* 2017; The Financial Markets Law Committee: *Issues of Legal Uncertainty Arising in the Context of the Withdrawal of the UK from the EU – The Application of English law, the Jurisdiction of English Courts and the Enforcement of English Judgement:* December 2017; and *Issues of Legal Uncertainty Arising in the Context of the Withdrawal of the UK from the EU – The Provision and Application of Third Country Regimes in EU Legislation:* July 2017; ISDA: *Brexit – CCP Location and Legal Uncertainty:* August 2017 (pages 6-8); and AFME: *Impact of Brexit on Cross-Border Financial Services Contracts:* September 2017.

27. Bank of England Financial Policy Committee, 25 September 2017.

28. Bank of England: "Continuity and freedom of contract are safeguarded. The introduction of the euro will not have the effect of altering any term of a contract, or discharging or excusing performance, or entitling a party unilaterally to alter or terminate the contract, subject to whatever the parties may have agreed.": *Practical Issues Arising from the Euro:* 14 December 1998.

Location, supervision and systemic risk

The European Commission has proposed that, as a result of Brexit, the framework for the recognition of third country – ie non-EU – central counterparties (CCPs) and their supervision needs to be enhanced, because of the "potential risks to the EU's financial stability".[29] Under the Commission's proposal, ESMA, in agreement with the relevant central banks, will recommend to the Commission whether or not a non-EU CCP is of "substantial systemic importance". If so, the Commission will then have the power to decide whether or not the CCP should be required to relocate activities within the EU27 as a condition for obtaining the regulatory approvals needed to operate in the EU Single Market.[30]

In a similar way, ESMA has published a cross-sectoral opinion on supervisory convergence and three opinions on sector-specific principles on relocations from the UK to the EU27 relating to investment firms, investment management and secondary markets in response to Brexit. ESMA's opinions are concerned with two main points. First, "firms need to be subject to the same standards of authorisation and ongoing supervision across the EU27 in order to avoid competition on regulatory and supervisory practices between Member States".[31] Second, delegation (eg of investment management) and outsourcing of market activities beyond the EU27 by firms authorised to operate in the EU27 need to be overseen and properly supervised from within the EU27.[32]

There are differing views about the links between the location of CCPs and systemic risk. The ECB has argued that CCPs have become effective vehicles for reducing systemic risk in the financial system, and the challenge is to ensure that they do not themselves become a risk to financial stability;[33] and the Governor of the Banque de France has argued: "Do not let sources of systemic risks for the EU grow outside the EU."[34] The alternative view is that clearing does not need to take place in the jurisdiction in which a financial asset is denominated, as central bank swap agreements can counter any systemic risks, and it is more efficient to clear on an international basis, regardless of currency, because this allows firms to net their risk in different currencies.

If mandatory relocation of derivatives contracts in CCPs from London to the EU27 is required by the EU27 authorities, it would involve costs and risks for users of capital markets, given current economies of scale in London from pooling liquidity in several currencies, which allow multilateral netting of transactions and a reduction in the collateral needed.[35] There is also a risk that mandatory relocation would cause market disruption, particularly if relocation is not properly organised over a sufficient period of time; and there may be implications, not just for the UK, but for the US and other third countries.

But if sufficiently robust arrangements can be established between the UK and the EU27 supervisors, mandatory relocation may not be needed. The ECB's concern is that "the current EU regime regarding third-country CCPs was never designed to cope with major systemic CCPs operating from outside the EU."[36] As a potential solution, the Governor of the Bank of England has proposed that cross-border arrangements for the supervision of CCPs "should be based on deep cooperation between jurisdictions and authorities who defer to each other's regimes where they meet international standards and deliver similar outcomes."[37]

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29. CCPs play a critically important role in providing the market infrastructure for managing risk. Market firms are required to clear certain derivatives trades through CCPs authorised for the activity concerned, and CCPs are also used to clear other products (eg repo), where use of CCPs is discretionary rather than mandatory. Most central euro-denominated clearing currently takes place in London as an international financial centre.

30. European Commission proposal to amend EMIR, 13 June 2017. In addition, the ECB is seeking to amend its Statute so that it has clear legal competence in the area of central clearing.

31. It remains to be seen whether there will be competition between different national competent authorities in the EU27 (eg for the relocation of financial services business). Commissioner Dombrovskis said in Tallinn on 15 September: "We think that national supervisors in the EU should follow the same supervisory priorities." See also the European Commission Communication, *op. cit.*, 20 September 2017.

32. ESMA: *Opinion on General Principles to Support Supervisory Convergence in the Context of the UK Withdrawing from the EU:* 31 May 2017; and *Sector-Specific Principles on Relocations from the UK to the EU27:* 13 July 2017.

33. Benoit Coeuré, Member of the Executive Board of the ECB: *European CCPs After Brexit:* GFMA, Frankfurt, 20 June 2017.

34. François Villeroy de Galhau, Governor of the Banque de France: FESE Convention, 22 June 2017.

35. ISDA has estimated that "a requirement that euro-denominated interest rate derivatives be cleared post-Brexit in an EU-based CCP would result in an overall initial margin increase in the range of 15 to 20%": Letter to Commissioner Dombrovskis, 8 June 2017.

36. Benoit Coeuré, Member of the Executive Board of the ECB: *European CCPs After Brexit:* GFMA, Frankfurt, 20 June 2017.

37. Mark Carney, Governor of the Bank of England: *A Fine Balance:* Mansion House speech, 20 June 2017. See also the Chancellor of the Exchequer: "We acknowledge that there are legitimate concerns among our EU colleagues about the oversight and supervision of financial markets here in the UK that are providing vital financial services to EU firms and citizens. We will address them by making forward-leaning proposals for greater transparency, cooperation, and agreed standards based on international norms. But, let me be clear, we will not accept protectionist agendas, disguised as arguments about financial stability. We will seek to agree new mechanisms around key issues, from dispute resolution to data protection.": UK Finance Dinner, 13 September 2017.

[continued from page 11]

UK to be workable upon Brexit, the European Commission would need to make the assessment before Brexit takes place.

25 *Authorisation in both the UK and the EU27:* If it is not possible to rely solely on regulatory equivalence, the other option is for firms involved in the international capital markets to be authorised, capitalised and staffed in both the UK and the EU27, where that is not the case already.[38] This would increase costs for international capital market firms, which would need to operate from two jurisdictions in Europe rather than one,[39] and could complicate the task for supervisors.[40] As a condition for providing authorisation to operate in the EU27, the question is whether – and to what extent – EU27 supervisors would insist on relocation of capital market activities and the market infrastructure from the UK to the EU27 on the grounds that location within the EU27 is necessary to ensure financial stability, or whether an acceptable alternative would be an agreed form of coordination between UK and EU27 supervisors over capital market activities and the market infrastructure needed to support them, where these are located outside the EU27 (eg in London). Clearly, the UK and EU27 supervisors would need to agree that the supervisory arrangements would be sufficiently robust to ensure that financial stability would not be put at risk. Indeed, avoiding financial instability would be one of the main reasons why coordination between supervisors would be necessary.

(iii) Capital market regulation after Brexit

26 When Brexit takes place, as capital market regulation in the UK and EU27 will be the same, there should be an opportunity for the UK and the EU27 to negotiate a free trade agreement which would provide mutual recognition of each other's regulatory regime.[41] In this respect, the UK will be unlike any other third country, because it starts from a position in which its regulatory and supervisory system is the same as the EU27, whereas other third countries have a different regulatory and supervisory background. Mutual recognition of the regulatory equivalence provisions in existing EU capital market legislation would not on its own be sufficient to achieve this, as there are gaps which would need to be filled. The free trade agreement between the UK and the EU27 could fill these gaps.[42]

27 Mutual recognition of regulatory equivalence would mean that regulatory provisions in the UK and EU27 would need to continue to be comparable in future after Brexit, while allowing the UK and the EU27 to implement agreed outcomes in their own way; and that there would also need to be provisions in the free trade agreement for enforcement and for settling disputes.[43] However, that should be less difficult to achieve in future than it would have been in the past, for two reasons. First, there is less new financial regulation in the pipeline now, as so much has been introduced in response to the crisis already. Second, in so far as further new regulatory initiatives are needed, they are likely to originate at global level from the G20 through the FSB, BCBS and IOSCO, which will affect both the EU27 and the UK in the same way, and in which both the EU27 and the UK will have a say.

38. In the EU27, this would normally be through subsidiaries. In the UK, it needs to be clear whether branches would be an acceptable alternative to subsidiaries. See Andrew Bailey: "Even if UK firms lose passporting rights to the European Single Market after Brexit, we should do what we can to maintain inwards activity into the UK": 19 July 2017.

39. Boston Consulting Group (for AFME) estimates that "approximately €1,280 billion of bank assets may need to be re-booked from UK to EU27 following a hard Brexit, unless alternative arrangements can be agreed. These assets are supported by €70 billion or approximately 9% of the (Tier 1) equity capital of the banks affected.": *Bridging to Brexit: Insights from European SMEs, Corporates and Investors:* AFME, June 2017. Oliver Wyman estimates that costs for banks will increase by up to 4% and capital requirements by up to 30%: FT, 1 August 2017.

40. Letter from the Head of the Prudential Regulation Authority to the Treasury Select Committee, 8 August 2017.

41. The alternative approach would consist of regulatory divergence after Brexit, which would risk leading to a regulatory "race to the bottom". This approach was implicitly rejected in the British Prime Minister's Florence speech on 22 September, in which she said: "We share a commitment to high regulatory standards."

42. An alternative might be the adoption of an Equivalence Regulation in the EU27 and reciprocal UK measures, if feasible in time. See Barnabas Reynolds: *A Template for Enhanced Equivalence:* Politeia, 10 July 2017.

43. The British Government has proposed a number of options, including a new UK/EU27 legal body that takes account of the European Court of Justice's rulings (like the EFTA Court), but ends the "direct" jurisdiction of the European Court of Justice in the UK: August 2017. In her speech in Florence on 22 September, the British Prime Minister said: "It would not be right for one party's court to have jurisdiction over the other. But I am confident we can find an appropriate mechanism for resolving disputes."

Conclusions

- There are five main ways in which to develop capital market integration across the EU: completing the programme of new EU measures under CMU; ensuring that existing EU measures are fit for purpose; achieving greater supervisory convergence across the EU; sharing risks across the EU to promote financial stability; and developing and integrating the financial market infrastructure.

- The prospects for CMU would be improved if accompanied by policy changes to strengthen the economic pillar of Economic and Monetary Union. This would involve agreement in the euro area on a path to fiscal integration. But it would also depend on resolving two specific issues which are closely related to CMU: the completion of Banking Union; and the search for a European safe asset as a euro benchmark.

- The question posed by Brexit is whether capital market integration is solely of benefit to the EU27 across national borders *internally* in the EU27, or whether open and competitive markets would benefit the EU27 *internationally* as well, and also be consistent with ensuring financial stability.

- Given the long lead-times for capital market firms in preparing for Brexit, agreement on a transition period needs to be reached by the UK and the EU27 as early as possible before Brexit to cover the period after Brexit until a free trade agreement is reached. Capital market firms will also want to be confident that they will need to make changes only once, and that they have a clear idea of the changes required.

- To avoid the risk of uncertainty about the continuity of cross-border financial contracts between market participants in the UK and the EU27, if passporting ends when Brexit takes place, the UK and EU27 authorities need to reassure the market by announcing as soon as possible that existing contracts outstanding when Brexit takes place will be "grandfathered", for example by providing for this in the UK/EU27 withdrawal agreement.

- There are two main options for capital market firms operating in the UK and the EU27. One is to rely on mutual recognition of regulatory equivalence. But this is currently a patchwork. The other is to be authorised, capitalised and staffed in both the UK and the EU27, which would increase costs for firms and could complicate the task for supervisors.

- As a condition for providing authorisation to operate in the EU27, the question is whether – and to what extent – EU27 supervisors will insist on relocation of capital market activities and the market infrastructure from the UK to the EU27 on the grounds that location within the EU27 is necessary to ensure financial stability, or whether an acceptable alternative would be an agreed form of coordination between UK and EU27 supervisors.

- When Brexit takes place, as capital market regulation in the UK and EU27 will be the same, there should be an opportunity for the UK and the EU27 to negotiate a free trade agreement which would provide mutual recognition of each other's regulatory regime, by filling in the gaps in the current regulatory patchwork. Regulatory provisions in the UK and the EU27 would need to continue to be comparable in future after Brexit, with provisions for enforcement and for settling disputes.

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By Catherine Wade

Benchmark reform and the future of LIBOR: implications for the primary bond markets

Summary

Regulatory reform relating to benchmarks has been ongoing for many years but the speech delivered by Andrew Bailey, the Chief Executive of the UK's Financial Conduct Authority (the FCA), on the *Future of LIBOR* on 27 July 2017 triggered increased focus from market participants.

The UK FCA have set a deadline of the end of 2021 after which it will no longer persuade or compel banks to submit data for LIBOR. Alongside this, from 1 January 2018, the European Benchmark Regulation (the BMR) will require certain entities to include robust fall-back plans in contractual documentation, dealing with the demise of an in-scope benchmark.

Here we focus on the impact of regulatory reform and the potential demise of LIBOR (in particular) on the primary bond markets.

Background

The key takeaway from Andrew Bailey's statement is that the FCA, as regulator of LIBOR, will not use its influence or legal powers to persuade or compel the panel banks that submit contributions to the benchmark to make submissions after 2021.

The speech made it clear that market participants will need to (i) develop alternative benchmark rates, and (ii) ensure that there are sufficiently robust fall-back arrangements for contracts entered into now that extend beyond 2021 (when it may well be that LIBOR will cease to exist in its current form).

Data submitted by panel banks for LIBOR is increasingly based upon expert judgment rather than actual transaction data because of the lack of active underlying markets to support the submissions. The FCA stated that this is unsustainable and undesirable for market participants. As a result, many panel banks are uncomfortable providing submissions which are based upon their judgment rather than actual transaction data, given the potential liability this creates.

However, the FCA, which regulates LIBOR, is currently able to compel submitting banks to provide submissions to avoid market disruption. Although the FCA has not yet been required to use its powers of compulsion, it has expressed concern that, once the provisions of the upcoming BMR apply, its powers will be limited.

By giving the market a timeframe to work towards, the hope is that it can allow for a planned and orderly transition away from LIBOR.

This timeframe has simply expedited existing workstreams

The review of major interest rate benchmarks has been ongoing for many years as part of the Financial Stability Board's initiative on interest rate reform. Following the Wheatley Review of LIBOR in 2012 and the Financial Stability Board report on *Reforming Major Interest Rate Benchmarks* in 2014, the three main administrators (EMMI for EURIBOR, ICE for LIBOR and JBA for TRIBOR) have been working on strengthening existing reference rates and developing alternatives. A number of "risk-free rates" are being identified and developed as alternatives to certain benchmarks, including sterling LIBOR.

However, by publicly announcing an end date after which

the FCA intends to stop persuading or compelling banks to submit LIBOR, the speech will accelerate workstreams that were already under way to find alternatives.

European Benchmark Regulation

Separately the BMR is due to apply in the EU from 1 January 2018. This Regulation will impose specific requirements upon administrators of and contributors to benchmarks, as well as to users of benchmarks. The broader remit of the BMR is outside the scope of this article but there is one provision in particular which is relevant to our consideration of fall backs in the case of the permanent discontinuance of LIBOR.

Article 28(2)

Pursuant to Article 28(2) of the BMR, a supervised entity that "uses" a benchmark will be required to have "robust written plans" in place setting out what actions will be taken if a benchmark materially changes or ceases to be available and to reflect such plans in its "contractual relationship with clients". LIBOR is a benchmark for these purposes.

What is a supervised entity? Supervised entities are certain types of EU regulated entities including credit institutions and investment firms.

What is "use"? Use has a specific meaning under the BMR but it can be assumed that use would include the issuance of a bond that uses a benchmark to calculate interest payments. Acting as a dealer under a debt issuance programme or an underwriter for a bond issuance alone is unlikely to bring an entity within the scope of "use" for the purpose of the BMR. It is also unlikely that an investor, by simply holding a bond referencing an in-scope benchmark such as LIBOR, would fall within the remit of Article 28(2) of the BMR. However, if a supervised entity has a role in relation to an issuance which involves determining amounts payable under financial instruments that reference a benchmark, for example as a calculation agent, that entity could be in scope.

What are the relevant contractual documents where this robust written plan should be set out? For a supervised entity as an issuer of bonds which reference a benchmark, the relevant client is the bond investor and so the relevant contract is likely to be the terms and conditions of the bond. A calculation agent appointed in connection with a bond issuance could also be caught by these provisions and so such agent would also need to ensure that robust contractual provisions are set out in the appropriate contractual documentation.

What do market participants need to do now?

There are two key questions that we are focusing on now: (i) a long-term alternative to LIBOR as a reference rate for floating rate notes; and (ii) interim measures for transactions being documented now with maturities extending beyond 2021, as well as fall back provisions for Article 28(2) of the BMR.

A separate issue will be legacy bond transactions which reference LIBOR and which have maturities extending beyond 2021. These same questions will arise in due course for transactions referencing other IBORs if it becomes apparent that they will no longer be published.

What are the long-term alternatives to LIBOR and other IBORs?

The five currency sub-groups (sterling, euro, Swiss franc, dollar and yen) formed by the Financial Stability Board Steering Group are responsible for driving the change to risk-free rates. These groups have each been tasked with identifying risk-free rates which could be used as alternatives to the IBORs.

In the UK, the Bank of England's Working Group on Sterling Risk-Free Reference Rates have announced SONIA (the

There are two key questions that we are focusing on now: (i) a long-term alternative to LIBOR as a reference rate for floating rate notes; and (ii) interim measures for transactions being documented now with maturities extending beyond 2021.

The absence of effective coordination and consideration of the impact upon the full product range could lead to basis risk, fragmentation and market disruption for issuers and investors alike.

Sterling Over-Night Index Average) as the preferred alternative benchmark to LIBOR for use in sterling derivatives and relevant financial contracts.

SONIA is the main benchmark for overnight unsecured money market transactions (brokered in London and denominated in sterling). Whilst not entirely free from credit risk (and, so, only a proxy for a truly risk-free rate), it incorporates lower credit risk when compared with longer tenors (where the window in which a default may occur is greater). As an overnight rate, SONIA does not have a maturity curve.

The Bank of England's Working Group on Sterling Risk-Free Reference Rates published a White Paper, *SONIA as the RFR and Approaches to Adoption,* in June 2017. ICMA has submitted a response highlighting the importance of ensuring contractual continuity for outstanding legacy debt securities and minimising market disruption.

In the US a broad Treasuries repo financing rate has been selected as an alternative by the relevant working group, the Alternative Reference Rates Committee (ARCC). In contrast to SONIA this is a secured rate. It is also worth noting that this rate is not yet being published.

In relation to the euro area, the risk-free overnight rate has not yet been identified. Under the administration of EMMI, much work has been done with the intention to strengthen the governance of EURIBOR and anchor it more firmly in transactions, yet we understand that challenges remain. On 21 September, the Financial Services and Markets Authority (FSMA), The European Securities and Markets Authority (ESMA), the European Central Bank (ECB) and the European Commission announced the launch of a new working group tasked with the identification and adoption of a risk-free overnight rate which can serve as a basis for an alternative to current benchmarks used in a variety of financial instruments and contracts in the euro area. The signatory public authorities emphasised the need for careful transition planning and safeguarding of continuity of contracts and reiterated that existing rates must continue to be provided in a robust and reliable manner. No deadline has been, or indeed may ever be, set for the demise of EURIBOR.

ISDA and its members are actively working on these long-term alternatives to the IBORs and to a certain degree the bond market and other markets will need to be guided by the derivatives market workstreams to establish IBOR fall backs and alternatives, given the inter-connectivity of the markets and the importance of ensuring matching cashflows between bonds and swaps. However, as mentioned in ICMA's response to the Bank of England White Paper, it will be important that the relevant working groups consider the financial markets as a whole and the full spectrum of products utilising the IBORs as a reference rate when determining the appropriateness of alternative rates. The absence of effective coordination and consideration of the impact upon the full product range could lead to basis risk, fragmentation and market disruption for issuers and investors alike. At ICMA, we are liaising closely with the UK authorities and other trade associations in this regard.

What are the differences between the IBORs and a risk-free rate?

The IBORs are based on unsecured interbank lending and therefore a proportion of the rate reflects the perceived credit risk (ie the premium charged by a lender to account for the risk that a borrower will not repay). By contrast, risk-free rates seek to isolate the interest rate without the credit element. The various currency working groups will need to consider how to adapt an overnight risk-free rate, or indeed a secured rate, to formulate an alternative to a forward-looking term IBOR incorporating a credit risk element.

Until the market lands on a mechanism for producing a robust alternative to the current IBORs that can be used as a reference rate for floating rate notes in the long term, bond market participants need to consider what actions to take in relation to transactions happening now.

What interim measures should the market adopt?

In the plain vanilla bond market long-term floating rate notes are not hugely prevalent, with many having a maturity of less than three years.

However, long-term securities referencing IBORs are more common in the context of regulatory capital for banks, with for example reset provisions from fixed to floating rate, corporate hybrid issuance, insurance regulatory capital and in the securitisation market.

How do bond terms and conditions referencing IBORs work?

There is no standard master form of terms and conditions for the international bond market. This is in contrast to the derivatives market which uses the various ISDA definitions. There is, however, a great deal of communality in the drafting of the relevant provisions in bond terms and conditions, with the outcomes being broadly consistent.

Currently the most common provisions found in bond terms and conditions are known as "ISDA determination" or "screen rate determination". Depending upon which option is selected by the bond issuer, the relevant fall backs which would apply in the event of a failure or termination of a chosen benchmark are set out in the contractual documentation as a waterfall of options. If the reference rate cannot be determined by application of the first specified fall back, the following applicable fall back applies and so on until the final fall back is reached.

Each of screen rate determination and ISDA determination provisions has a different fall-back waterfall. Screen rate determination is the more prevalent.

Taking each of these two options in turn:

(i) *Screen rate determination:* ie the IBOR rates quoted on the relevant screen page plus or minus a margin. Where the rate is not published on the relevant screen, the provisions provide for a fall back to various iterations of rates to be determined by reference banks and finally a fixed rate using the last available floating rate for the life of the bonds. A fall back to reference banks may not be effective if an IBOR is permanently discontinued. The relevant reference banks are likely to include the same or a similar group of banks to those that are no longer submitting data to allow for LIBOR to be published on the relevant screen. In any event, these fall backs are only intended for a temporary period as, in the case of a permanent discontinuance of a reference rate, it would effectively result in instruments becoming fixed rate.

(ii) *ISDA determination:* This typically refers to calculation on the same basis as the floating rate leg of an interest rate swap for the relevant designated maturity, determined by the calculation agent on the basis of the ISDA definitions. If the bond issuer has a swap in place to exchange the cashflows on the notes for another stream, then it makes sense for these to match. If this is the chosen option, the fall back will be to ISDA fall back provisions.

There may also be variations on these alternatives described, as well as different historic provisions in documentation in relation to legacy floating rate notes.

ICMA is participating in data gathering on the volume of long term outstanding floating rate notes to quantify the challenges in relation to legacy trades. However, any such high-level data will not give granular information on the specific bond terms and conditions that apply to those legacy bonds.

What are the options for new bond issues or debt issuance programmes updating now prior to a long-term solution?

Screen rate determination

In the case of a screen rate no longer being available on the relevant screen the fall-back provisions could defer to a successor or replacement screen.

At present any alternative rate chosen for LIBOR, for example, is not expected to be published on the same screen and it is also unlikely that it will be considered a "successor" to LIBOR (but this could depend upon the specific drafting of the bond terms and conditions and final outcome of the deliberations of various working groups and ISDA). Providing for the alternative rate to be published, or at least referenced on the screen that is currently used, could facilitate a smoother transition to an alternative rate.

As an alternative, a bond issuer could use a revised fall-back waterfall now to add an additional fall back providing for the issuer, calculation agent, trustee or independent third party to make a determination based upon what is customarily used in the market as an alternative screen or alternative benchmark at the time required. This assumes that in due course, and by the time the relevant IBOR is no longer published and an alternative is required, there will have been a clear determination by the market of what the alternative benchmark should be. However, whilst there remains uncertainty as to the direction of travel on alternatives, some may consider that this gives too much flexibility for the issuer, which could be detrimental to bondholders. In the case of a third party there may well be reluctance to take on liability for making this determination. There may eventually be no one clear alternative applicable to all outstanding securities.

Another alternative or additional last resort approach in the fall-back waterfall could be for issuers to provide for easier amendments to interest rate provisions, in the future, in the bondholder meeting provisions to allow for a liability management exercise once an alternative benchmark is established. Finally, an issuer could choose to use an alternative reference to LIBOR or the relevant IBOR from the outset.

Using an alternative reference rate from the outset

At this stage work in relation to the various risk-free rates to enable them to be used as an alternative to an IBOR for a new bond issue is insufficiently advanced. In the case of SONIA, this is an overnight rate which is backward looking and does not include credit risk. SONIA alone will result in an economically different outcome to LIBOR.

It is difficult for market participants to pre-judge the outcome of the on-going work on the risk-free rates to produce an interim or long-term rate as any alternative to the relevant IBOR.

For market participants looking to other alternative reference rates that could be used by a bond issuer now, it will be important to select a rate with certainty that this reference will continue to be available in the long-term future. One such reference could be government bond yield curves plus a spread, instead of an IBOR. Another option could be to use an alternative screen rate which does not defer to an IBOR definition or other rate that may cease to exist.

ISDA determination

Similar options to those described above could also apply to ISDA determination provisions.

These provisions typically defer to the 2006 ISDA definitions but market participants could use language to incorporate any future amendments to the relevant ISDA definitions in relation to IBOR fall backs in the event that the relevant IBOR ceases to exist.

We understand that ISDA is working on amendments to its 2006 definitions, among others, to address the permanent discontinuance of the IBORs. We also anticipate that ISDA will use a protocol mechanism to provide for amendments to existing contracts for those that elect to adhere to the amendments. At this stage, using drafting which incorporates future amendments to ISDA definitions could introduce too much uncertainty or result in unintended consequences for issuers and or bondholders.

Risk factors

Some issuers are taking the precaution of introducing additional risk factor language to highlight any risks that may are as a result of the demise of LIBOR (or other IBORs), as appropriate. Any such risk factor would need to be carefully worded and tailored to the specific circumstances of the bond terms and conditions. A risk factor alone would not address the outstanding questions highlighted above and there remains some debate about the relevance or value of a risk factor, particularly for wholesale debt issuances or programmes targeted at sophisticated investors for whom such a risk factor is unlikely to be informative.

Legacy issues

Unlike in the derivatives market, changes to pre-existing bond terms and conditions cannot be made via a protocol mechanism. Amendments to legacy bond terms and conditions would typically require a liability management exercise such as a consent solicitation. This could be costly and time consuming for issuers and with an uncertain outcome. An alternative mechanism could be some form of coordinated statutory measure in the main jurisdictions. However, this is potentially complex to deliver.

Conclusion

At ICMA we are actively engaged with the relevant authorities. We are also coordinating with other trade associations to facilitate a market wide approach to documentation. We are seeking feedback from members via relevant committees as to appropriate short-term and long-term alternatives to relevant IBORs, as well as robust fall-back provisions; and working with external law firms to reflect market practice in bond documentation. Our current sense is that there is not yet a consistent approach to new bond documentation, with decisions being made on a case-by-case basis. We will continue to monitor developments and facilitate member engagement and solutions for the market.

We will keep members updated via future editions of the ICMA Quarterly Report, member briefings, and our committees as necessary.

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The state and evolution of the Asian cross-border corporate bond markets

By Andy Hill and Mushtaq Kapasi

In August 2017, ICMA, under the initiative of its Secondary Market Practices Committee (SMPC), began its study into the state and evolution of the Asian cross-border corporate bond markets. Similar to previous work conducted by the SMPC related to the European corporate bond market, the focus is very much on the developments and forces impacting the secondary market. In particular the study seeks to identify key trends and changes in market structure and participation, as well as exploring the effects of regulation and monetary policy in light of these trends and developments, and how, in combination, this is impacting market evolution, efficiency, and liquidity.

The study is largely qualitative in approach, and based on extensive interviews with market participants and stakeholders, including sell-side and buy-side firms, intermediaries and infrastructure providers, issuers, as well as regulators and policy makers. ICMA has already conducted a number of interviews in the region, and encourages its APAC members who have not yet participated to contribute to the study. ICMA will look to finalise its report in the first half of 2018.

The Asian cross-border corporate bond markets

What becomes clear from preliminary interviews is that there is no "Asian" corporate bond market as such; rather, there are multiple local markets, which are largely heterogeneous and idiosyncratic in nature, structure, and participation. To this extent, the focus of the study is very much on the international, cross-border segments of the regional credit markets. In practice, this is primarily the regional USD corporate bond market, although, increasingly, the onshore renminbi (CNY) market is establishing itself internationally.

The regional USD corporate bond market currently stands at around $850 billion, of which a little more than $500 billion[44] is made up of financial issuance (largely banks). In terms of non-financial corporate (NFCs) issuance, Australian issuers dominate for now, followed by Indonesian, Japanese, Korean, Singaporean, Hong Kong, Indian, and Malaysian issuers, while Chinese banks constitute the largest source of financials issuance, comfortably eclipsing Australian and Japanese financials.

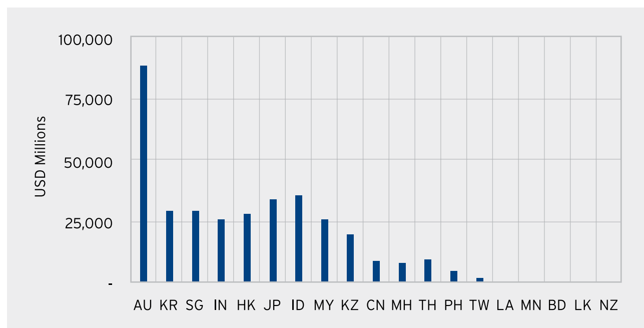
Primary market liquidity

From the preliminary interviews, it would seem that the Asian USD market is in good health, with growing net issuance, new regional issuers coming to the market, and larger issues. As one respondent pointed out, five years ago the common issue size for an investment grade (IG) entity was around $500 to $750 million. Today, it is not unusual to see issues in the $2 to $4 billion range.

44. Based on RegS issuance by APAC incorporated financial entities.

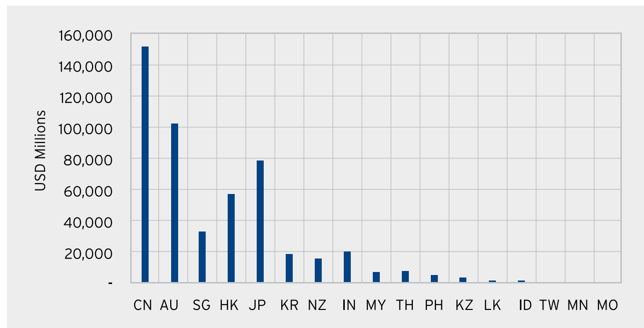
Regional demand is also buoyant. Whereas historically large marque issues would require a 144A tranche to ensure full participation, these days large issues are almost exclusively issued under RegS. In fact, the story seems to be that supply is not keeping up with demand for regional USD corporates, particularly as dollar-rich Chinese onshore funds become a larger part of the regional investor base. A common concern is that this demand-supply imbalance is affecting valuations, with spreads at levels that are difficult to rationalise.

Outstanding APAC USD denominated NFCs (Total $354.2bn)



Source: Bloomberg

Outstanding APAC USD denominated Financials (RegS) (Total $502.8bn)



Source: Bloomberg

Secondary market liquidity

So far, the interviews paint a mixed picture with respect to secondary market liquidity. Some respondents (both sell-side and buy-side) suggest that secondary market liquidity is poor, mainly as a result of small overall market size, a tendency for regional investors to "buy and hold", and the reduced capacity for the traditional global banks to provide meaningful market-making services. However, other respondents maintain that, at least in relative terms, liquidity is comparable with the US and European markets, with ticket sizes of $10 to $20 million easily executable, tight bid-ask spreads, and an increased pool of regional market makers without the capital constraints of their international competitors.

Financing and hedging markets

The discussions so far point to concerns about the absence of deep and liquid repo and credit default swap (CDS) markets, which, to an extent, also affects market efficiency and liquidity. It has been highlighted that many regional investors are not actively involved in the securities lending or repo market, mainly due to legal and contractual barriers, which limits supply to support secondary market making. As one buy-side respondent explained, either investors accept settlement fails as normal, or market makers cannot provide offer-side liquidity in bonds they do not already hold.

The lack of a meaningful single name-CDS market is attributed to a number of factors, not least the fact that credit spreads are tight, and volatility low, which makes hedging less cost effective. The increased capital constraints of traditional market makers further supress activity.

E-trading

The ongoing electronification of the European credit markets is a key theme of ICMA's work, and a major focus of the study is on the uptake of new platforms and e-protocols in the Asian markets. The initial feedback seems to be that the region is moving relatively slowly in this respect. One electronic trading venue dominates, although there is some growing traction with other established US and European platforms. But ultimately, the Asian credit markets are very much over-the-counter. Relationships and personal networks are fundamental to market functioning, and, as one respondent suggested, the trust and integrity of counterparties is a critical dynamic. One interviewee used the expression "a human dark pool" to describe the structure of the Asian markets. Accordingly, trading platforms are used mainly for smaller transactions, or for supporting post-trade processes following OTC execution; thus, usage is driven more by efficiency and compliance requirements, rather than for sourcing liquidity.

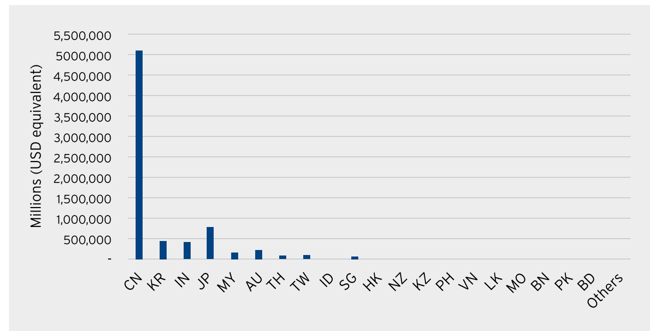
There is no "Asian" corporate bond market as such; rather, there are multiple local markets.

Local currency markets

To the extent that local currency (LCY) markets form part of the cross-border flow, the study is very much interested in the structure and development of these markets. While access to many markets remains limited, and secondary market liquidity poor, the greatest potential for "internationalisation" appears to lie with the onshore CNY market, particularly with the introduction of the Bond Connect initiative. While activity has been relatively muted since its launch in July 2017, this is widely expected to accelerate, noting that the Chinese onshore corporate bond market is second in size only to the US.

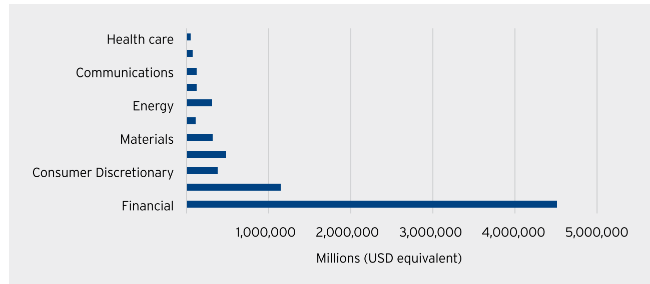
However, respondents have so far highlighted a number of potential barriers that international investors will need to address. In a market where 85% of issuers are rated AAA, proprietary analysis of credit risk is essential, which could be a challenge for smaller investors. A lack of market transparency could also be a concern for some investors, while legal issues related to governance and bankruptcy could prove to be a deterrent for others. Some respondents also note the dominance of financial issuers, where transparency around leverage is a key concern, and that the market still lacks a depth of quality NFC credits. That said, the general view toward the opening-up of the onshore market is markedly optimistic.

Outstanding APAC LCY corporates by county of issuance (Total $7.5tn)



Source: Bloomberg

Outstanding APAC LCY corporates by sector (Total $7.5tn)



Source: Bloomberg

Continuing the study: member participation

The above observations are a summary of the main discussion points coming out of preliminary interviews with market participants and stakeholders, and the final report will discuss all of these issues and more in far greater depth, reflecting a broader range of commentary and viewpoints. ICMA encourages those members who are not already engaged in this study to contact either Mushtaq Kapasi in ICMA's Hong Kong office, or Andy Hill in ICMA's London office who are leading the research, and who would be keen to facilitate interested members' participation.

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Bond Connect: a new channel into China's onshore bond market

By Julien Martin and Mushtaq Kapasi

The Bond Connect scheme, launched on 3 July 2017, is the most recently introduced link between securities markets of mainland China and Hong Kong, following the Shanghai- and Shenzhen-Hong Kong Stock Connect schemes introduced in 2014 and 2016 respectively. China's domestic bond market has grown 20 per cent annually since 2012, and has now reached $10 trillion in outstanding notional size, to become the world's third largest bond market after those of the United States and Japan. Although foreign investment in China's domestic bond market has been allowed through various access channels since 2002, foreign ownership still accounts for only 2 per cent of the total market. Bond Connect introduces structural and procedural improvements intended to expand the global investor base and the share of foreign ownership.

Bond Connect is regulated jointly by the People's Bank of China (PBOC) and the Hong Kong Monetary Authority (HKMA). Bond Connect currently allows "north-bound" trading (ie investment from Hong Kong into mainland China), which effectively opens up the China interbank bond market (CIBM) to all overseas investors. "South-bound" trading (ie allowing mainland Chinese investors to invest in offshore bond markets) will be explored at a later stage.

In the two months since the inception of Bond Connect, 164 foreign investors have been approved to participate in this new investment channel. This is compared to 473 foreign investors approved over the last 15 years under the three bond access channels in existence before Bond Connect, namely the Qualified Foreign Institutional Investor (QFII) scheme launched in 2002, the Renminbi QFII (RQFII) scheme launched in 2011 and the CIBM Direct scheme launched in 2010.

Since the launch of Bond Connect, overall foreign investor holdings in Chinese domestic debt securities, as reported by China Central Depository & Clearing Co., Ltd. (CCDC) and Shanghai Clearing House (SHCH), have increased by RMB 122 billion ($17 billion).

Features of Bond Connect

- *Market admission criteria and process:* The investor admission criteria for Bond Connect follows the admission criteria in the China Interbank Bond Market (CIBM) Direct scheme set out by the PBOC. However, under Bond Connect, overseas investors can submit bilingual applications through Bond Connect Company Limited, a joint venture between China Foreign Exchange Trade System (CFETS) and Hong Kong Exchange (HKEX). The overall processing time for new investors is expected to be 10-12 working days.
- *No quota or mandated investment plan:* For Bond Connect, there is no investment quota (unlike the QFII and RQFII schemes) or requirement for investors to file an investment plan detailing the intended size of investment (unlike the CIBM scheme).
- *Trades denominated in CNY:* Investors can participate in the Bond Connect using renminbi or foreign currency.

Market participants are closely monitoring whether the new Bond Connect scheme could increase the likelihood of benchmark index inclusion for onshore China bonds.

If foreign currency is used, the investor can convert currency through Hong Kong settlement banks with access to the onshore FX market. Investments under Bond Connect will be denominated in onshore renminbi (CNY), unlike investments in the Stock Connect schemes which are denominated in offshore renminbi (CNH). Portfolio managers using Bond Connect will therefore not exposed to currency basis, which is relevant to the compilation of emerging market bond indices.

- *Trading efficiency and enhanced execution:* Under Bond Connect, investors have access to CIBM cash bonds in both primary and secondary markets, through a trading link established between recognised access platforms and CFETS. Investors can directly trade through a familiar interface of international fixed income trading platforms on an electronic request-for-quote (RFQ) basis, and are free to request a quote from any of the currently 24 participating onshore dealers. This is an improvement from the CIBM Direct scheme, in which an investor can only trade Chinese bonds through an onshore bond settlement agent bank.
- *Onshore FX hedging:* Under Bond Connect, investors now can hedge their bond positions on FX and rates in the onshore and offshore markets. In addition, unlike the QFII or RQFII schemes, there are no capital repatriation limitations under Bond Connect.
- *Settlement and custody: offshore nominee holding structure with fully-secured holding:* Bond Connect establishes a settlement link between onshore and offshore central securities depositories: China Central Depository and Clearing Co. (CCDC) along with Shanghai Clearing House (SCH) on the Chinese mainland, and HKMA's Central Moneymarkets Unit (CMU) in Hong Kong. Investors can appoint offshore global custodians, or CMU members as local custodians, and the purchased bonds will be held in custody under a nominee structure with the CMU. The end-investors are the beneficial owners of the bonds purchased under Bond Connect, and will have bondholder rights and enforcement rights related to the relevant bonds.
- *The nominee holding structure* adopted by Bond Connect is similar to the structure widely used in the international markets. Under the CIBM scheme, investors must open direct onshore settlement accounts with the CCDC and SCH.

Future enhancements

Bond Connect, like Stock Connect before it, is expected to be enhanced over time, in particular with the addition of new access platforms, new products such as repo and CNY derivatives, and "south-bound" trading.

As Bond Connect improves the accessibility of the domestic Chinese bond market to foreign investors, market participants are closely monitoring whether the new Bond Connect scheme could increase the likelihood of benchmark index inclusion for onshore China bonds, playing a role similar to Stock Connect before the inclusion of Chinese A-shares in MSCI's emerging markets index in June 2017.

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Market electronification and FinTech

By Gabriel Callsen

Building on a previous article on market electronification[45] and FinTech that was published in the ICMA Quarterly Report Issue 46 in 3Q 2017, this article summarises a new ICMA paper which seeks to explore further the key drivers behind electronification of investment grade (IG) corporate bond markets and the impact on market structure, notably: (i) efficiency and straight-through processing, (ii) liquidity sourcing, (iii) regulatory compliance, and (iv) data management. In line with ICMA's continued engagement, the focus of the paper is on primary, secondary and repo markets in Europe. Findings are based on research, ICMA publications, internal discussions and conversations with ICMA member firms.

Market electronification varies significantly between IG corporate bond primary, secondary and repo markets. While all three are interrelated from a market perspective, there is a clear divide when it comes to the adoption of technology. Indeed, electronification in one area has not necessarily spilled over into other areas.

Efficiency considerations are key drivers for the adoption of technology in all three areas to some degree. In secondary markets, the increasing electronification of markets has been a result of technological advances, "the drive for cost efficiencies"[46] and Basel III's regulatory requirements.

In contrast, technology has to date had less of an impact on primary markets. There is a number of solutions automating processes at different stages of the issuance cycle. However, it is noteworthy that new initiatives based on distributed ledger technology (DLT) continue to emerge, *inter alia*, for issuing bonds or Euro Commercial Paper.[47]

Credit repo markets have to date been impacted far less by technological advance than secondary markets, while regulation has hampered trading activity. Indeed, it is considered a "highly manual, labour intensive market"[48], but a gradual adoption of technology has been observed in certain areas.

In the post-trade lifecycle of bonds, the use of technology is widespread, but at the same time remains fragmented. Whether for collateral management, corporate actions or reconciliations, a myriad of systems is available for interlinked, yet different processes.

The ICMA ERCC Ops FinTech Working Group has conducted a mapping exercise of over 50 technology solutions which is being finalised and will be published in the near future. Perhaps unsurprisingly, the use of DLT in this area is considered to generate the greatest benefits in terms of efficiency gains and cost reduction.

Beyond efficiency considerations and cost savings, liquidity (or rather the lack thereof) remains a major concern in secondary markets and is a key driver in the evolving landscape of electronic trading. A visible trend is the emergence of information networks which aggregate dealer inventories and aim to match up potential trading interests, rather than facilitate execution via the traditional RFQ model. Examples can be found in the ICMA ETP mapping directory.

Regulatory compliance, another key factor, is driving further electronification and the adoption of solutions in secondary and repo markets, and, to a lesser extent, primary markets. MiFID II/R and SFTR impose far-reaching reporting and order record-keeping requirements on market participants.

45. Defined as "rising use of electronic trading technology", BIS, 2016. The scope of this paper extends beyond trading technology and includes post-trade technology.

46. ICMA: *Evolutionary Change: The Future of Electronic Trading in European Cash Bonds*, 2016 (page 3).

47. A non-exhaustive snapshot of DLT-related initiatives in fixed income can be found in the full paper on ICMA's website.

48. ICMA: *A Study into the State and Evolution of the European Credit Repo Market*, 2017 (page 28).

Set to take effect on 3 January 2018, MiFID II/R extends pre- and post-trade transparency requirements to bond markets. While SFTR already entered into force on 12 January 2016, the reporting requirements were subsequently adopted on 31 March 2017 and will only apply once the technical standards are in place. The reporting obligation is expected to enter into force at the earliest from 1Q 2019 in a phased approach.

Fuelled by regulatory requirements, technology solutions designed to help market participants comply with regulation, referred to as "RegTech", are becoming more and more important. While the use of technology is not new, the data-driven approach adopted by regulators is one of the key drivers of electronification.

In terms of data management, the unprecedented level of publicly available data across fixed income markets under MiFID II/R will pose a twofold challenge for secondary market participants. On the one hand, firms will be obliged to capture an array of internal data to comply with regulatory requirements. On the other, technological capabilities to source and aggregate trading data, and feed these into internal risk and pricing systems, will be critical to both the buy side and the sell side.

In primary markets, the availability of data on secondary market activity is expected to have less of an impact. However, in credit repo markets and post-trade processing, capturing data will become equally important and probably more challenging since trades are predominantly executed over-the-counter.

DLT initiatives have gained further traction in recent months, notably in niche sectors such as private placements and the area of post-trade. It is expected that DLT solutions will be rolled out to the market within the next six to twelve months. While it is too early to gauge the take-up and impact on market structure, there is a sense of inevitability that DLT will be adopted sooner or later.

Notwithstanding the trend towards electronification, fixed income markets are underpinned by trust and human relationships. It is therefore worth pointing out that the adoption of technology solutions will not replace, but rather complement human interaction. Indeed, it will remain vital, and technology can help make more efficient use of time and focus on nurturing relationships.

It will be interesting to see how market electronification will evolve in light of the proliferation of new FinTech initiatives, the new regulatory landscape under MiFID II/R and SFTR and increased transparency in bond markets from January 2018. What is clear, however, is that technology will become more important than ever before.

The full paper, which is available on ICMA's website, discusses all of these findings in greater depth.

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Technology solutions designed to help market participants comply with regulation, referred to as "RegTech", are becoming more and more important.

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:

Primary markets

1 *Issuers:* The Public Sector Issuer Forum is meeting at the World Bank in Washington on 12 October to discuss cybersecurity and LIBOR replacement, among other issues. The Corporate Issuer Forum and the Financial Institution Forum met in London on 21 September and 4 October respectively.

2 *Prospectus Regulation:* With the support of the ICMA Legal & Documentation Committee and leading international law firms, ICMA responded to the ESMA consultation paper on Level 2 measures on the Prospectus Regulation by the 28 September deadline.

3 *MiFID II/R implementation in primary markets:* ICMA continues to work with members in the ICMA Primary Market Practices Committee and the Legal & Documentation Committee, the Asia Bond Syndicate Forum and Asia Legal & Documentation Forum, on the implications for the primary markets of the forthcoming MiFID II/R regime (for product governance, justification for allocations, and inducements) and PRIIPs regime.

4 *Future of LIBOR:* Following the statement by the FCA on 27 July that banks will only be obliged to contribute to LIBOR until the end of 2021, ICMA is working with members, international law firms and other trade associations on the implications. ICMA held a conference call for members on the future of LIBOR on 7 September, led by Catherine Wade and Ruari Ewing: 430 members joined the conference call.

Secondary markets

5 *European Commission Expert Group on Corporate Bond Market Liquidity:* ICMA is represented by Andy Hill on the European Commission High Level Expert Group on Corporate Bond Market Liquidity. The Expert Group is finalising its recommendations this autumn. The European Commission's consultants on corporate bond market liquidity made a presentation to ICMA's Secondary Market Practices Committee at its meeting on 18 September.

6 *IOSCO:* ICMA is responding to the IOSCO consultation on corporate bond market transparency by the deadline of 16 October, and is in contact with IOSCO about ICMA's research on corporate bond market liquidity (or lack of liquidity) in stressed market conditions. ICMA also participated in a panel on MiFID II/R at the Affiliate Members Consultative Committee (AMCC) of IOSCO in Mumbai on 25 September.

7 *MiFID II/R implementation in the secondary markets:* ICMA is holding a series of workshops for members this autumn. They began in Stockholm on 6 September, and continued in Brussels on 4 October, Luxembourg on 5 October and Paris on 6 October. Further workshops are planned in Madrid on 19 October, Frankfurt on 26 October and Milan on 27 October. ICMA has also held workshops in Hong Kong and Singapore. The workshops focus on the implementation of MiFID II/R and the implications for fixed income trading.

8 *Single name CDS study:* Jointly with ISDA, ICMA will be conducting a study into the state and evolution of the European single name credit default swap market.

9 *Asian corporate bond liquidity study:* ICMA has been researching the state and evolution of the Asian corporate bond markets, as an extension of its work on the European markets, with plans for a separate report to be published in early 2018.

10 *ICMA Secondary Market Rules & Recommendations:* ICMA is reviewing the impact of MiFID II/R on its Secondary Market Rules & Recommendations.

11 *European investment grade bond market data:* Historical data on bond market trading activity, split between financials and non-financials, in both euro and sterling, can now be accessed on the ICMA website.

12 *ETP Mapping Directory:* The ICMA Electronic Trading Platform (ETP) Mapping Directory, which has recently been updated, provides a single source of information on over 30 infrastructure providers and is available on the ICMA website.

Repo and collateral markets

13 *ICMA credit repo study:* ICMA has published a new research study, *The European Credit Repo Market: The Cornerstone of Corporate Bond Market Liquidity.* The study was prepared by Andy Hill as a joint initiative of the ICMA European Repo and Collateral Council (ERCC) and ICMA Secondary Market Practices Committee.

14 *Collateral pledge structures:* ICMA is working with members to explore a few cases where the use of collateral pledges may help boost the extent and efficiency of market activity. This may lead to work on incremental market standard documentation.

15 *MiFID II/R and the repo market:* ICMA is continuing to work on clarifying the extent to which repos and other securities financing transactions (SFTs) are in scope of MIFID II/R. It has been confirmed that pre- and post-trade transparency, most transaction reporting and some of the critical best execution requirements under RTS 27 will not apply to SFTs.

16 *SFTR implementation:* ICMA is continuing to help members to implement the Securities Financing Transaction Regulation (SFTR), and is promoting members' involvement in a bilateral reconciliation exercise to identify the most critical reporting elements requiring further industry work.

17 *Post-trade:* With the support of its ERCC Committee and its Operations Group, ICMA is working to respond to the European Commission consultation on post-trade. This reflects the conclusions of the European Post-Trade Forum, in which the ERCC has been represented.

18 *ECB AMI-SeCo:* The ERCC is represented on the ECB's recently formed Advisory Group on Market Infrastructure for Securities and Collateral (AMI-SeCo). Among other things, this group is taking forward work on collateral management harmonisation which was initiated in the forerunner COGESI group. ICMA is actively involved.

19 *Repo and the real economy:* The ERCC is planning to hold its next biannual General Meeting in Brussels on 14 November. Discussions will highlight the importance of repo for the real economy. Speakers include Benoit Coeuré from the Executive Board of the ECB, Mahmood Pradhan from the IMF, Jochen Metzger from the Bundesbank and Steffen Kern from ESMA.

Asset management

20 *AMIC Excom:* The Executive Committee of the ICMA Asset Management and Investors Council (AMIC) met at AXA in Paris on 27 September, and exchanged views with Benoit de Juvigny, Chief Executive of the Autorité des marchés financiers (AMF).

21 *Leverage and asset management:* Jointly with EFAMA, the AMIC has published a report on fund leverage as a contribution to the continuing debate (eg between the FSB and IOSCO) on systemic risk and asset management. The report analyses how leverage is used and how the European legislative framework regulates leverage, and makes recommendations to improve the monitoring and analysis of leverage risk.

22 *ETFs:* The AMIC has responded to the Central Bank of Ireland consultation on exchange-traded funds (ETFs), and focused on the potential for systemic risk from ETFs and the impact of ETFs on corporate bond market liquidity.

23 *Liquidity risk management:* On 18 September, the AMIC responded to the IOSCO consultation on liquidity risk management, welcoming IOSCO proposals for revisions to its 2013 liquidity risk guidelines, but suggesting improvements in fund level stress tests. ICMA participated in a panel on liquidity risk management at the IOSCO-AMCC meeting in Mumbai on 25 September.

24 *MiFID II/R research unbundling:* Following agreement with the AMIC Executive Committee, ICMA is conducting a fixed income-focused survey for asset managers on the implementation of the MiFID II/R proposals on research unbundling.

Capital market products

25 *European Commission Expert Group on Sustainable Finance:* ICMA is represented by Nicholas Pfaff as an observer on the European Commission High Level Expert Group on Sustainable Finance.

26 *Green finance in Asia:* ICMA has provided feedback to the Green Finance Committee, under the auspices of the People's Bank of China, on the development of Chinese green bond policy; made recommendations to the ASEAN Capital Markets Forum on south-east Asian securities regulation related to green finance; and commented on a Hong Kong green bond policy paper drafted by Our Hong Kong Foundation, a Government-related think tank.

27 *Award for Social Bond Principles:* The Social Bond Principles, voluntary guidelines that recommend transparency and disclosure for bonds raising funds for social projects, have received the award for the most important innovation in 2017 for the SRI bond market from Global Capital.

28 *Infrastructure finance:* Jointly with AFME, ICMA (represented by Katie Kelly) published a report on *European Infrastructure Finance: A Stock-take*. The report analyses current infrastructure financing, investment and relative initiatives, and assesses how to advance and encourage further private sector finance for infrastructure projects.

Other issues

29 *Brexit:* ICMA has continued to keep in contact on Brexit with the UK, the euro area and the EU authorities, and to discuss with members – both in the UK and the EU27 – through ICMA Market Practice and Regulatory Policy Committees how it can best help the international capital markets to prepare.

Other meetings with central banks and regulators

30 *DG FISMA:* The ICMA Regulatory Policy Committee exchanged views with Niall Bohan of the European Commission (DG FISMA) on Capital Markets Union and related issues at its meeting in Brussels on 21 September.

31 *Official groups:* ICMA continues to be represented, through Martin Scheck, on the ECB Bond Market Contact Group; through René Karsenti, on the ESMA Securities and Markets Stakeholder Group; and through Godfried De Vidts on the ECB Macroprudential Policies and Financial Stability Contact Group, and on the Consultative Working Group to ESMA's Secondary Markets Standing Committee.

Primary Markets

by Ruari Ewing, Catherine Wade and Kate Craven

Omnibus III and prospectus approvals

On 20 September, the European Commission published a 283 page proposal for a new Regulation (Omnibus III) on the European Supervisory Authorities (ESAs – EBA, EIOPA and ESMA), together with a related 184 page impact statement and shorter press release and fact sheet. Feedback is also invited by 16 November.

Inter alia, the proposal provides (at pages 239-240) that the new Regulation would transfer, from national regulators to ESMA, the approval of certain prospectuses under the Prospectus Directive (PD) – namely those regarding (i) admissions to qualified investor-only regulated markets (or such specific segments thereof), (ii) asset-backed securities, (iii) "specialist" issuers (property, mineral, scientific research-based and shipping companies) and (iv) non-EU third country issuers. It also provides (at page 236) that the new Regulation would also transfer to ESMA the advertisement powers relating to the offers and regulated market admission requests covered by such prospectuses.

Whilst a single European regulator has been envisaged generally, it is not clear why these particular prospectus changes are being singled out and at this time, particularly given the preceding Commission consultation (to which ICMA responded in May) and feedback statement made no mention of prospectuses.

It is important that EU policy making is evidence-based. In this respect, the Commission notes that ESMA's existing convergence work has been "unable to promote supervisory convergence and the landscape of prospectus approval requirements remains fairly fragmented across the EU" and that there is "also a risk of supervisory arbitrage as issuers might target national CAs which they consider less demanding in order to get approval for prospectuses." However, ESMA's convergence work is not completed (presumably at least partly because the European co-legislators constantly change the underlying rules), with risk factors for example due to be covered in 2018. And furthermore, it is not clear that market users perceive actual challenges to market operation and investor protection in this respect – regarding qualified investor-only regulated markets at least, European regulatory philosophy considers that such investors require less protection than other investors (indeed offers to qualified investors-only require no prospectus approval at all). The reference to arbitrage as a hypothetical possibility is telling in this respect – there are many hypothetical risks to market resilience, but presumably good regulation principles contemplate that new rules should address circumstances where detriment has actually occurred or is likely to do so (based on evidence).

The Commission also notes: "many national CAs would have to hire prospectus readers with the skills to deal with these relatively rare types of prospectuses" and "duplication of resources in different national CAs for a few cases only". However, such a burdening of resources is not pre-ordained. Several national regulators are highly experienced in approving prospectuses in specific contexts and issuers of debt securities with denominations of €1,000 or more are already able to choose in this context any national regulator that satisfies the PD's nexus criteria. The Commission also notes that in the context of the "United Kingdom's exit from the Union, Luxembourg might be faced with a disproportionate workload" – but this again seems to be general hypothesising (unless Luxembourg's CSSF has expressed concerns in this respect).

The Commission also notes that the PD's current advertisement regime provides for fragmented supervision across host national regulators. However, such supervision could be concentrated with the current home national regulator that approved the related prospectus.

A key aspect would be the ability of ESMA to deliver a seamless transition by approving prospectuses at the same level of efficiency (in terms of speed, predictability and cost) as the most efficient national regulators currently do (also bearing in mind third country listing options such as New York, Dubai, Singapore and Hong Kong). This is particularly

so given the constant stream of ongoing disruption being faced by the markets as the wall of new EEA regulations (MiFID II, PRIIPs, Benchmark Regulation, etc) continues to be delivered. Such a seamless transition would presumably involve significant budgetary and human resourcing implications (including in terms of specific legal/sectoral/linguistic expertise) and the Commission acknowledges generally (ie even without focusing on a seamless transition) that the "personnel implications of a move toward central ESMA approvals of certain wholesale and ABS prospectuses could be considerable".

Regarding specialist issuers specifically, there may also be logistical challenges with transferring approval to ESMA as the "specialist" nature of such issuers is not always initially apparent (so an approval application might be initiated with a national regulator, then suspended part-way as specialist status is recognised and then re-started at the ESMA level). Regarding qualified investor-only regulated markets/segments, the Commission states these are "expected to develop and grow over time, potentially amounting for a significant number of future wholesale non-equity prospectuses". However, the concerns above regarding seamless transition may result in issuers preferring to continue seeking national regulator approval of prospectuses with €100,000 denominations, which would undermine the Prospectus Regulation's Level 1 purpose of granting regulatory recognition to such qualified investor only regulated markets/segments.

Ultimately, the proposal for transferring prospectus approval to ESMA seems to run clear risks in the pursuit of hypothetical gains – and so more concerns for the future of European primary markets that ICMA will seek to feed back to the Commission.

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EU Prospectus Regulation

ICMA submitted its responses to the ESMA Level 2 consultations on *Format and Content of the Prospectus* and *Scrutiny and Approval of the Prospectus* on 28 September. The responses are in line with our previous communications on the Prospectus Regulation. Ruari Ewing and Catherine Wade spoke at the IFLR 8th Prospectus Rules Conference on 26 September, which included speakers from the European Commission, ESMA and a number of national regulators as well as industry experts.

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PRIIPs and MiFID II/R product governance

ICMA continues to work on anticipated approaches, in the Eurobond markets (ie syndicated cross-border bond issuance), to the product governance (PG) and PRIIPs regimes coming into effect from 2018. These approaches would not purport to be exhaustive or exclusive, but are anticipated to be useful to the extent transaction parties wish to minimise deal/syndicate-level deliberations, to maximise execution efficiency and speed (bearing in mind that many seasoned borrowers today are able to mandate a syndicate of underwriters to then price a benchmark-sized new issue within hours intra-day).

Background

It may be helpful to recap briefly on the PG/PRIIPs regimes by way of background. For PRIIPs, simplifying substantially: (i) any person manufacturing a "packaged" product, before it is "made available" to retail investors in the EEA, must publish a key information document (KID) and then regularly review it, and if needed, publish a revised KID; and (ii) any person advising on, or selling, such a product must provide retail investors in the EEA with the KID in good time before those retail investors are bound by any contract or offer. For PG, simplifying substantially: (i) MiFID II persons that "create, develop, issue and/or design financial instruments, including when advising corporate issuers on the launch of new financial instruments" are "manufacturers" for PG purposes (with co-manufacturing documented in an agreement); (ii) MiFID II persons that "offer or sell financial instrument[s]" are "distributors" for PG purposes (with no connection to the manufacturer being explicitly required); (iii) manufacturers must identify, and communicate to distributors, a compatible target market of investors and periodically review that target market; and (iv) distributors must identify their own target markets (by either adopting manufacturer's target market or refining it) – all on a "proportionate" basis.

Neither regime "grandfathers" pre-existing bonds and there has been limited consensus on what does *not* constitute a "packaged" product. This is partly due to various public statements by the European Commission and ESMA that seemingly purport to widen the range of what might otherwise have been perceived as "packaged". Practically in the context of syndicated bond issuance, borrowers are understood to be manufacturers for both PRIIPs and (if a MiFID II person) PG purposes (together with, as co-manufacturers for PG purposes only, any MiFID II person underwriters that satisfy the related "advising" characteristic). Though post-2018 "distribution" of pre-2018 bonds is subject to the PRIIPs (if "packaged") and PG regimes, the "manufacturing" of such bonds, however, occurred prior to the PRIIPs and PG regimes coming into effect.

Challenges

Significant practical/logistical challenges are perceived regarding: (i) borrower liability risk in producing a KID in the context of high value / flow transaction bonds (let alone keeping it up to date); and (ii) underwriters' scope to execute extensive target market review procedures, particularly on a co-manufacturer basis that is effectively syndicate/ ISIN-specific and given traditional market practice whereby borrowers engage (and remunerate) underwriters for the initial issuance procedure only.

Some of these concerns may abate with practical experience of the new regimes and any future helpful official guidance, but the approaches ICMA is working on seek to account for them in the interim – by focusing on manufacturers: (i) being clear that they are not facilitating availability to retail investors in the EEA of any products that are not outside the scope of PRIIPs' "packaged" concept; and (ii) defining "robust" target markets for PG purposes – ie that are highly likely to endure for the life of a bond and so substantially moderate the ongoing (review process) resourcing burden, this seemingly being simplest in first instance to outline in a proportionate wholesale context of professional investors.

PG professional investors intended target market

On the basis that professional investors (as defined in MiFID II, including elective professionals and discretionary managers) possess the experience, knowledge and expertise to define their needs and objectives, make their own investment decisions and properly assess and manage the risks and returns that they incur, they should be able to buy and hold any bond investment, regardless of specific product type, and therefore the manufacturer of a bond should have then substantively complied with the PG regime if it ensures that measures are put in place on issue that are reasonably expected to result in sales only being made to such investors (and see further below).

Because professional investors are appropriate target investors for all bond types, this will continue regardless of any changes individual bonds over time. In this respect, manufacturer target market reviews of the bond markets would most likely (if not inevitably) conclude that no target market changes are warranted – at least whilst the MiFID definition of professional investors endures. In this respect, feedback from third party "distributors" (in the specific PG sense) would be expected to be without impact on the target market assessment.

A negative target market is unlikely for most bonds given diversification/portfolio considerations and absent the exercise of regulatory intervention powers. However, any such negative target can be subject to consideration in the specific circumstances.

A written agreement between co-manufacturers seems likely (beyond generally acknowledging the PG regime and the professional investors target market approach) to address any desired ongoing logistical role attributions. Some co-manufacturer groups may consider in this respect that no specific role attributions are necessary: ie that all tasks be effectively equally shared. Other co-manufacturer groups may wish perhaps to attribute the task of initially receiving any distributor feedback (no matter how unlikely to materialise) and consequentially notifying the other co-manufacturers, as well as defining a technical means of conferring/deciding on any co-manufacturer proposal to amend the target market (again no matter how unlikely to materialise).

Options for measures reasonably expected to result in sales only to professional investors

Various options are available for consideration in terms of measures that might be put in place on issue that could, in varying combinations according to the circumstances, be reasonably expected to result in sales only being made to professional investors. Furthermore in this respect, manufacturers should not then be characterised as "making available" to retail investors in the EEA any "packaged" securities for PRIIPs purposes. The more salient options could include line items in any origination staff formalities e-mail in response to mandate, in any term sheet and/or in any sales staff memorandum, legends in any prospectus and any final terms or pricing supplement and on new issue screens, selling restrictions in any prospectus and any final terms or pricing supplement, counterparty procedures (including in terms of any secondary trading involvement), the absence of a retail prospectus or of a KID, admission to a "qualified investor" segment on an EEA regulated market, MiFID trader PG obligations, markers on market/trading screens and high denominations. ICMA is working on model forms of wording relating to some of the above. However, these are not anticipated to involve debt issuance programmes to be updated on an emergency basis prior to 2018.

Retail investors intended target market

ICMA is also continuing to consider potential target market approaches for retail investors (and to engage with EU and national authorities in this respect). However, public offers conducted on behalf of EEA governments at least have presumably a mass retail target market (on an initial and ongoing basis) as a matter of public policy (EEA government bonds are also exempted from the PRIIPs regime).

Conclusion

ICMA will continue to focus on the PRIIPs and PG regimes with its committees and keep members updated.

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ICMA Corporate and Financial Institution Issuer Forums

by Katie Kelly

Fulfilling a need to ensure full market representation and to complete the suite of ICMA issuer forums, the ICMA Corporate Issuer Forum (CIF) was inaugurated in March 2013 with a high-quality membership which has grown into a powerhouse of frequent corporate issuers.

Although its membership spans Europe, the CIF meets three times each year in London with agendas formulated to ensure broad appeal to a cross-section of different interests depending on what is topical, but ensuring that there is "something for everyone", often with the involvement of external experts and other ICMA groups (such as the Asset Management & Investors Council and the Primary Market Practices Committee). New issues processes are of perennial interest to all issuers – in particular allocations, disclosure of the order book, investor soundings and the potential effects of regulations such as MiFID II/R and MAR. Given the volumes of corporate activity, issuers also have an opportunity to discuss interesting transactional features, concerns or other relevant considerations at the meetings.

Owing to the confidential, non-competitive, non-deal context environment, issuers are very candid in voicing their concerns, challenges and market and transaction experience. This has led to a high level of trust developing between the members and makes for a friendly and easy dynamic.

The ICMA Financial Institution Issuer Forum (FIIF) is comprised of the main frequent issuing European banks and operates on a similar basis to the CIF, albeit with a different, more bank-focused agenda. Recently, a group for FIIF Treasury Counsel was established with a view to supporting the FIIF members, working with them to highlight and prioritise relevant issues and suggesting and developing output for the group. The first of its kind, this group, known as the Treasury Counsel Group (TCG) also ensures that treasury counsel individuals are familiar with the areas where ICMA is most active in primary markets, meaning that its members will benefit from ICMA's expertise, resources and networks.

According to discussions between ICMA and various regulatory authorities, the issuer voice is often under-represented when considering the necessity for, and the effects of, regulatory interventions. With the support of ICMA, the CIF and the FIIF are encouraged to engage with regulatory authorities, including by way of presenting joint positions and inputting into consultations, allowing ICMA to present a comprehensive, rounded industry view for the authorities and for other ICMA members. This helps to ensure that the CIF and the FIIF become entrenched in the mind of regulators and others as the "go-to" group for market leadership, innovation, influence and issuer guidance.

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Asset-Backed Commercial Paper

On 6 July, the BCBS and IOSCO released the consultative document, *Criteria for Identifying Simple, Transparent and Comparable Short-Term Securitisations*, for comment by 5 October. These short-term STC criteria maintain and build on the principles in the *Criteria for Identifying STC Securitisations* issued by the BCBS and IOSCO in July 2015. They take specific account of the characteristics of Asset-Backed Commercial Paper (ABCP) conduits, such as (i) the short maturity of the commercial paper issued, (ii) the different forms of programme structures and (iii) the existence of multiple forms of liquidity and credit support facilities. The criteria aim to assist the financial industry in its development of STC short-term securitisations. They were designed to help the parties to such transactions to evaluate the risks of a particular securitisation across similar products and to assist investors with their conduct of due diligence on securitisations.

Alongside of this, the BCBS released the consultative document, *Capital Treatment for Simple, Transparent and Comparable Short-Term Securitisations*, also for comment by 5 October. This sets out additional guidance and requirements for the purpose of applying preferential regulatory capital treatment for banks acting as investors in, or as sponsors of, STC short-term securitisations, typically in ABCP structures. The additional guidance and requirements include that: (i) investors have access to key monthly information on the performance and key characteristics of the ABCP structure; (ii) the redemption risk of the underlying assets is addressed from the sponsor's perspective; and (iii) the transactions funded by the conduit have an enforceable legal structure and that the relevant information is disclosed by the sponsor to investors.

The proposed treatment is consistent with the BCBS's July 2016 revisions to the securitisation framework. The 2016 standard sets out additional guidance and requirements for differentiating the capital treatment of STC term securitisations from that of other securitisations. Similarly, provided that the proposed criteria are met, STC short-term securitisations will receive the same reduction in capital requirements as other STC term securitisations. This aims to enhance the framework's risk sensitivity without significantly increasing banks' operational burden in computing the applicable capital relief.

Industry feedback to this consultation has been quite extensive, with a wide range of detailed suggestions regarding how best to achieve the objective of putting in place a strong and workable framework. It must be hoped that officials will prove to be open to adaptation of the consultation proposals in line with this feedback, as there are significant concerns regarding the achievement of this objective. For instance, the industry's view is that it appears to be impracticable for any ABCP sponsor to comply with the currently proposed conduit-level criteria.

Circulated on 31 May, AFME's 2Q 2017 Securitisation Data Report shows that European ABCP issuance was €68.4 billion in 2Q 2017. This is a further decline of 16.9% versus the prior quarter and of and 43.0% versus the prior year. Multi-seller conduits (97% of total), particularly from France, continue to dominate as the largest category of issuer in the ABCP market.

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It appears to be impracticable for any ABCP sponsor to comply with the currently proposed conduit-level criteria.

Secondary Markets

by Andy Hill, Elizabeth Callaghan and Gabriel Callsen

MiFID II/R FAQ: impact on non-EU/EEA secondary bond market participants

MiFID II/R background

The Markets in Financial Instruments Directive (MiFID) is a European Union law that provides harmonized regulation for investment services across the 31 Member States of the European Economic Area. The Directive's main objectives are to increase competition and consumer protection in investment services. MiFID became effective in November 2007, and primarily related to equities markets. MiFID II (along with the Markets in Financial Instruments Regulation – MiFIR),[49] replaces MiFID, and broadens its scope to non-equities, including bonds. Among the key aspects of MiFID II/R are provisions covering: transaction reporting, market structure, pre-trade transparency requirements, post-trade reporting, best execution reporting, and conduct of business rules. MiFID II/R entered into force in July 2014 and *will apply in EU Member States from 3 January 2018*.[50]

The European Securities and Markets Authority (ESMA) was empowered to develop the numerous regulatory and implementing technical standards for MiFID II/R to support implementation, the majority of which having been adopted by the European Commission entered into law in early 2017.[51] ESMA is further publishing guidance and recommendations, in the form of "Q&As" (at Level 3) on various aspects of MiFID II/R over the course of 2017 to support implementation.[52]

The information contained herein has been provided by third-party sources and is intended for general information only (the "Information"), and is not intended to be and should not be relied upon as being legal, financial, investment, tax, regulatory, business or other professional advice. ICMA is not responsible for the accuracy, reliability, currency or completeness of the Information. ICMA does not represent or warrant that the Information is accurate, suitable or complete and neither ICMA nor its employees or representatives shall have any liability arising from, or relating to, its use.

Non – EU/EEA Secondary Markets Participants (extra-territorial)

Q1. To which entities does MiFID II/R apply, and to what extent is it intentionally extra-territorial?

In the same way that MiFID is not intended to be deliberately extra-territorial in scope, MiFID II/R is only intended to apply to EU investment firms and activities undertaken in the EU. In other words, it does not matter where a financial instrument is listed or traded, or where the client is based; if the EU MiFID authorised firm is based in the EU, then it is in direct scope of MiFID II/R, and if it is based outside of the EU (including subsidiaries of EU firms), then it is not in direct scope. A notable and explicit exception is *non-EU branches of EU MiFID authorised entities*, which *are* in scope of MiFID II/R reporting requirements, wherever they are based.

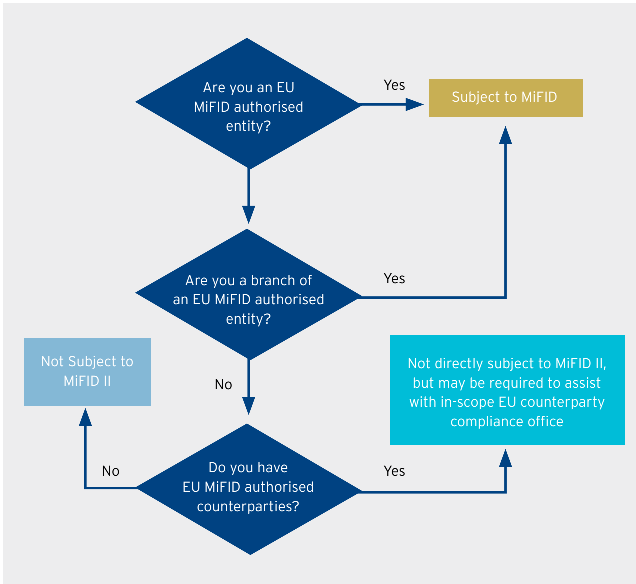
49. MiFID II is a Directive (that replaces MiFID), which is adapted and implemented at the Member State level. MiFIR is the Regulation that enforces MiFID II and applies at the EU level as it is. Elements of MiFID II may therefore vary slightly across different Member States (but not MiFIR).

50. Originally MiFID II/R had been scheduled to be applied in January 2017, but was delayed for twelve months in light of the implementation challenges facing both industry and regulatory authorities.

51. With respect to the MiFID II, Member States are expected to transpose the Directive into national law before 2018.

52. These can be found on the ESMA website.

However, while non-EU investment firms dealing with EU counterparties are not directly in scope of MiFID II/R, they may be indirectly impacted in a number of different areas that they will need to be aware of. With respect to secondary bond markets, important considerations when dealing with EU MiFID authorised counterparties will include providing information to support transaction reporting, the distribution of research, and product governance.



Q2. What are the obligations of non-EU firms for transaction reporting?

Branches of EU MiFID authorised investment firms are explicitly in scope of the transaction reporting requirements [RTS 22], even where the transaction is executed outside of the EU and regardless of where the instrument is listed. The reporting requirement will be to the Home State regulator of the EU parent entity.

For non-EU investment firms (including subsidiaries) that transact with an EU MiFID authorised counterparty, or on an EU venue, the transaction reporting obligation will be the responsibility of the EU counterparty or trading venue. However, the reporting venue or EU entity will be required to provide a significant amount of data (there are 65 separate reporting fields), including details relating to the counterparty. These will include the identification of the counterparty (in the form of its LEI code – see Q4), the name and date of birth of the executing trader, as well as the name and date of birth of the investment decision maker.

Q3. Are EU firms transacting on non-EU venues responsible for post-trade transparency?

MiFIR Articles 20 and 21 [RTS 2] require EU MiFID authorised firms to make public information on transactions through approved publication agreements (APAs), including transactions traded on a trading venue. In the case of trades executed on EU trading venues, the trading venue will provide this post-trade transparency. However, it is unclear as to whether EU firms are responsible for post-trade transparency in the case of executing trades on third-country (non-EU) trading venues.

ESMA has concluded that EU investment firms should not systematically republish information in the EU with respect to trades concluded on third-country trading venues that are subject to transparency provisions similar to those applicable to EU trading venues. Accordingly, ESMA is expected to publish a list of third-country trading venues that it considers meeting the criteria necessary for EU firms not to re-report trading information in the EU. It should be noted that third-country trading venues cannot apply directly to be on the ESMA list; rather EU firms are expected to nominate third-country trading venues for ESMA's assessment.

Q4. Are non-EU firms required to have LEIs?

While the transaction reporting requirements [RTS 22] fall on EU MiFID authorised entities and trading venues (see Q3), EU firms (and their non-EU branches) dealing with non-EU entities will be required to provide the Legal Entity Identifier (LEI)[53] of their counterparties, including non-EU

Non-EU firms that do not have an LEI by 3 January 2018 may find that EU counterparties are unable to transact with them, or that they are unable to transact on EU trading venues.

53. The Legal Entity Identifier is a unique 20-character, alpha-numeric code, that identifies a legal entity that engages in a financial transaction. LEIs are issued by Local Operating Units (LOUs) of the Global LEI system. LEIs are required for each separate legal entity.

counterparties. Therefore, non-EU firms that do not have an LEI by 3 January 2018 may find that EU counterparties are unable to transact with them, or that they are unable to transact on EU trading venues.

Similarly, *issuers* of securities that are traded on EU venues (Regulated Markets, Multilateral Trading Facilities, Organised Trading Facilities, and Systematic Internalisers) will also need LEIs, as trading venues are required to provide these as part of the instrument reference data for all instruments admitted to trading [Article 27].

Q5. Are non-EU firms subject to pre-trade transparency obligations?

MiFIR Article 8 [RTS 2] requires a pre-trade transparency obligation for bonds that are classified as liquid, and which fall below specified size thresholds with respect to Large-In-Scale (LIS) and Size-Specific-To-the-Instrument (SSTI). This will apply to quotes on venues, and, in the case of OTC quotes, to Systematic Internalisers (SIs) for the relevant instrument.

With respect to quotes provided on EU venues, the trading venue will be responsible for complying with the pre-trade transparency obligations. In terms of OTC transactions, since non-EU entities cannot be SIs, non-EU entities are not in scope of any pre-trade transparency obligations.

Q6. Are non-EU firms subject to post-trade transparency obligations?

MiFIR Article 21 [RTS 2] requires a post-trade transparency obligation for bonds for EU MiFID authorised firms and EU trading venues. The obligation to make public trade details will fall on the trading venue, for on-venue trades, including SIs. For OTC trades (not with an SI), the obligation will fall to the selling counterparty. Where bonds are classified as liquid, and the transaction sizes fall under the LIS and SSTI thresholds, trade data will be reported close to real time (under 15 minutes). For bonds that are not classified as liquid, or are above the LIS and SSTI size thresholds, the publication of post trade information will be subject to a deferral of between 2 days and 4 weeks, as determined by the relevant EU Home Country regulator. The trade data is made public through an approved publication arrangement (APA).

Since the post-trade transparency requirements fall on EU trading venues (including SIs) or EU investment firms, non-EU entities are not required to make public post-trade information.

Q7. If non-EU firms are not subject to pre- or post-trade reporting requirements, could they still be affected?

While the obligation to provide pre-trade transparency will fall on the EU trading venue (including SIs), a non-EU firm will need to be aware that any quote they receive from an SI (including non-EU branches) will be subject to pre-trade transparency requirements, and so will be publicly disseminated.

Similarly, while the post-trade transparency reporting obligation will not fall on a non-EU entity, in the event that the trade is executed on an EU venue, or is booked with an EU entity (or its non-EU branch), then the trade will be subject to the post-trade reporting requirements, and will be publicly reported. The non-EU entity may therefore need to take into consideration which EU Home Country reporting deferral regime is applicable in the case of large trades, or trades in illiquid securities, since this could impact pricing and liquidity.

Q8. Can non-EU firms become Systematic Internalisers?

The Systematic Internaliser (SI) regime is intended to extend the pre- and post-trade transparency obligations into the OTC space for non-equities (including bonds). EU MiFID authorised investment firms will be classified as SIs for a financial instrument where they deal on their own account, OTC, on an organised, frequent and systematic, and substantial basis in that instrument ("frequent and systematic" and "substantial" are defined quantifiable thresholds). Firms can also "opt in" to becoming designated SIs for particular financial instruments.

The broad understanding is that only EU domiciled entities can be designated SIs, so non-EU entities can neither qualify nor elect to be SIs. This includes the EU branches of non-EU entities.

However, the trading activity of non-EU branches of EU entities will be in scope of the "frequent and systematic" and "substantial" tests for the SI designation of the EU entity.

Q9. Are non-EU firms subject to best execution requirements?

Article 27 [RTS 27 and 28] requires EU MiFID authoirsed investment firms to take "all sufficient steps" to ensure best execution for their clients, and are required to disclose their best execution policy. Furthermore, EU execution venues (which include trading venues, SIs, market makers, and other liquidity providers) are required to make publicly available, on a regular basis, at no cost, extensive and highly detailed information to illustrate quality of execution. Investment firms are also required to publish annually information on the quality of education obtained for client orders on their top five execution venues.

The understanding is that the best execution requirements (including the related reporting obligations)

do not apply to non-EU firms, nor to the non-EU branches of EU firms, even when trading with an EU entity, and that the local best execution requirements of the relevant regulatory authority will apply.

However, it may be the case that EU firms dealing with non-EU entities request their best execution policies, and expect that these are in line with the policies generally adopted by EU investment firms.

Furthermore, non-EU entities may be asked for data points on transactions from their EU counterparts, because EU firms need such data to fulfil their top 5 execution venue reporting obligations under Article 27(6) (further specified in RTS 28).

Q10. What are the implications of research unbundling for non-EU firms?

MiFID II introduces new rules related to "inducements" and prohibits EU MiFID authorised firms[54] from receiving certain inducements, including free research. Therefore, EU firms are required to pay for research received, which, in the case of fixed income research, can be either from their own P&L or through the establishment of a Research Payment Account (RPA) which is funded by a direct charge to clients.

While this does not directly apply to non-EU firms, this has implications with respect to the provision and receipt of research, particularly for jurisdictions with different rules to the EU. It may be difficult for a non-EU firm to provide research to an EU firm since the EU firm will be obliged to pay for it. Non-EU research providers may therefore need to charge their EU counterparties for research that they currently provide for free. Furthermore, global EU MiFID authorised firms headquartered in the EU receiving research may decide to start paying for research outside Europe as well. These developments could present a particular problem for US entities, for example, since it is unlawful in the US for firms to charge for research without being registered as an investment advisor.[55]

In future, non-EU firms who have received research from EU firms in the past for free, may find that EU firms who have started charging for research for their EU clients, may start charging all their clients for research.

EU/EEA Secondary Markets Participants (intra-territorial)

Q11. Which EU National Competent Authority has jurisdiction over the trading activities and practices of a branch entity of an EU/EEA MiFID authorised firm?

The Competent Authority of the Member State where the branch is located assumes responsibility for ensuring that the services provided within its territory comply with MiFID II/R provisions: eg The deferral regime of the host Member State for that branch will apply (Branch of UK firm in Sweden: Swedish FSA MiFID II/R interpreted rules apply, *not* UK FCA interpreted rules)

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54. Note that some EU jurisdictions, such as the UK, are extending application from EU MiFID authorised firms to most UCITS and AIF funds registered in the UK, but this is not true for all jurisdictions.

55. At the time of writing, the SEC is understood to be looking at the possibility of creating a "carve out" to avoid this inherent conflict with MiFID II requirements.

MiFID II/R implementation: road tests and safety nets

With MiFID II/R's deadline looming, many firms are concerned that they may not have the optimal solution implemented on day one that meets both regulatory obligations and their firm's trading objectives. With this in mind, ICMA has some suggestions for road-testing new regimes and safety nets for new trading workflows to allay fears and assist in preparations for the MiFID II/R implementation date of 3 January 2018. These are based on the many interactive discussions in ICMA's MiFID II/R Working Group meetings.

SI regime "road testing"

The systematic internaliser (SI) regime[56] comes into effect in September 2018 (although investment firms may elect to "opt in" to the regime from 3 January 2018). Many thought it might have been quite useful in January to start "opting in" and "opting out" as much as firms wanted, in order to test the new SI regime in a live environment. However, this was deemed impractical as SIs would need to connect to their local regulator's data base to send reference data. Negative consequences could arise regarding the quality of the reference trade data, created from opting in and opting out. Therefore, opting in and opting out before September 2018 is clearly not the answer. Nevertheless, some sort of "road-testing" is needed.

The suggestion is therefore to create a "virtual" SI regime under which sell sides create various scenarios with clients and trade as if they were an SI (without opting into the regime) before September 2018. Firms must make clear to their clients that this is a road test and that they do not in fact have SI status. Some of the road-testing scenarios follow:

How to inform clients if you are an SI for a particular instrument, per legal entity and per currency:

- Individual approved publication arrangements (APAs)[57] are starting to collect the data. (As there will be no centralised database for SIs in order to replicate a centralised SI database, APAs will need to share the data they collect with all the other APAs.) While these databases are incomplete in the beginning, any of the identifier codes based on SIs, per instrument and per currency, will be useful to test. In this way firms can be ready for when this data is more fully available through the APAs.

How to provide firm pre-trade SI quotes publicly:

- A utility for publishing is the ideal, but some firms may end up posting spreadhseets (in the form of an "xls" file) on a website (this is still in machine readable format). That "xls" file on the website has to be tested with clients as if live.
- SI quotes will have an identifier. If a client wants to trade with an SI based on that quote, the client must identify that quote by its identifier. This procedure needs to be tested.
- OTC SI quotes that are subsequently executed on venue (usually via a "request for quote to one"- more on this further below). The SI quoting obligation is removed when the trade is executed on the venue, as venue obligations supersedes the SI. This needs to be reviewed and scenario-tested.

How to publish SI trades with SI flags:

- This is new. A pre-trade quote identifier will need to straight-through process (STP) to a post-trade flag. This is fine if you have an electronic trading system or an order management system (OMS)/execution management system (EMS) with FIX protocol.[58] However, it will be very challenging for local brokers who are used to voice trading and do not have systems that can handle SI trades that carry post-trade SI flags that MiFID II requires. A system

56. The systematic internaliser regime imposes pre- and post-trade transparency requirements for OTC quotes and transactions on investment firms which, on an organised, frequent, systematic, and substantial basis, deal on their own account by executing client orders outside of regulated market, Multilateral Trading Facility, or Organised Trading Facility without operating a multilateral system.

57. Approved publication arrangements (APAs) are entities authorised under the provisions established in MIFID II to provide the service of publishing trade reports on behalf of investment firms.

58. A Financial Information eXchange (FIX) protocol is an electronic communications protocol that facilitates international real-time exchange of information related to securities transactions and markets.

needs to be created to attach flags to the trade reports. Testing of this process is then required.

Final note: Some firms have not yet decided whether they will or will not be an SI. It would be useful to road-test (while not live) the SI regime fully and test the STP of the SI process, including legal entity identifiers (LEIs), IT systems (will they be ready in time?) and APAs. Not to mention the take-up of firm quotes, are clients actually trading as a direct result of SI quotes? By testing the full end- to-end SI process, firms will have the data to make a more informed decision as to whether or not they should become an SI, come September 2018.

"Safety net" for large or illiquid trades

Many say that market structure is all about providing "tools in the toolbox" for buy-side and sell-side traders to execute in a more streamlined and efficient manner. MiFID II/R is speeding up the progress of automation in fixed income markets. Come 3 January 2018, it also increases the likelihood of major growth in platform execution on MTFs and the new category of OTFs for liquid bonds. However, based on the discussions in ICMA's MiFID II Working Group, there is concern regarding trading workflow and market structure when it comes to large or illiquid trades in light of the new MiFID II/R rules.

The anxiety surrounding the new MiFID II/R-based trading workflow refers to buy sides not wanting the impact of information leakage that is caused by putting a large or illiquid trade (ie an order or trade in securities considered to be illiquid) out to multiple counterparties. If this information is prematurely released, the market can trade (or re-price) against the counterparties involved. An example is a large block trade in a jurisdiction with a very short timeframe for post-trade deferral. This causes market impact for the buy side and does not give the sell side enough time to trade out of its positions. The counterparties involved will prefer to trade report in a jurisdiction that protects them from the negative effects of premature trade reporting exposure.

In the MiFID II Working Group, several participants have mentioned that what is needed is the use of an existing "safety-net" that allows for large or illiquid trades to be negotiated off-venue and executed on-venue (this is through the existing "Request for Quote to One" or "RFQ to 1" protocol). The possible addition to this existing RFQ to 1 protocol is a trade flag for buy-side best execution purposes to demonstrate that this order/trade did not go out to multiple counterparties for price formation, in order to protect the trade performance.

Other benefits to this "off-venue/on-venue" trade protocol, apart from reduction in market impact for large or illiquid trades, are: (i) confidence in trade reporting accuracy, as the platform reports; (ii) the agreed quote is captured electronically, instead of on the phone; and (iii) straight-through processing migrates voice trading to electronic and creates an audit trail.

However, it is important to stress that this will use the existing RFQ to 1 protocol, with the possible addition of a flag for best execution purposes. Since this protocol only applies to large or illiquid trades, platforms that execute using this protocol must have the necessary waivers for large or illiquid trades. Everyone agrees that the platforms will have to benefit from a jurisdiction that has a four-week supplementary deferral regime in place.

ICMA is currently hosting discussions with market structure providers and the bond trading community to further develop and define this protocol in order to provide market participants with a "safety-net" for large or illiquid trades, come January 2018.

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MiFID II/R implementation: ESMA guidance

With less than three months remaining, MiFID II/R will enter into force on 3 January 2018. During the third quarter of 2017, the European Securities and Markets Authority (ESMA) has provided further guidance on a number of key issues for fixed income markets.

The following briefing is designed to provide a non-exhaustive summary of relevant guidance impacting market structure and fixed income trading, notably (i) transitional transparency calculations for bonds and credit derivatives; (ii) market structure, access to trading venues and CCPs; (iii) pre-trade transparency waivers, and (iv) MiFIR data reporting.

(i) MiFID II transitional transparency calculations for bonds and credit derivatives

To increase transparency in fixed income markets, MiFID II/R requires details of trades to be made publicly available. RTS 2, a delegated regulatory technical standard, sets out detailed pre- and post-trade assessment criteria for non-equity instruments including bonds and credit derivatives. The concepts of large-in-scale (LIS) and size-specific to the instrument (SSTI) define thresholds above which instruments are eligible for pre-trade transparency waivers and post-trade deferrals.

On this basis, ESMA published on 11 September 2017 threshold values for the various categories of bonds[59] which are deemed liquid. These will be valid for bonds and derivatives from 3 January 2018 until 31 May 2019, and will subsequently be updated once every year.

Bond Type	SSTI pre-trade	LIS pre-trade	SSTI post-trade	LIS post-trade
Corporate Bond	300,000	1,000,000	1,500,000	2,500,000
Convertible Bond	500,000	1,500,000	2,000,000	3,000,000
Other Public Bond	400,000	3,500,000	5,500,000	15,000,000
Covered Bond	300,000	1,500,000	3,000,000	7,000,000
Sovereign Bond	700,000	6,000,000	10,000,000	25,000,000
Other Bond	300,000	2,000,000	4,000,000	15,000,000

Note: Values are displayed in euro.

Liquidity assessments for individual bonds by ISIN are due to be released by 1 December 2017, as stated in the related FAQ on transitional transparency calculations.

With respect to credit derivatives, ESMA published an update on 11 September 2017 amending the initial calculations issued on 3 July 2017. Owing to erroneous data provided to ESMA by a trading venue, the number of credit derivatives considered liquid has decreased and includes only the iTraxx Europe 5-year and iTraxx Europe Crossover 5-year CDS indices. Rather than referring to a specific series, the assessment is based on maturity and encompasses respective indices with four to five years to maturity. This means that not only the on-the-run series, but also the previous series are deemed liquid.

59. Referred to as "sub-asset class" in the legislative texts, namely Corporate; Convertible; Other Public; Covered; Sovereign and Other bonds.

Underlying index	SSTI pre-trade	LIS pre-trade	SSTI post-trade	LIS post-trade
ITRAXX EUROPE 5Y	7,500,000	55,000,000	175,000,000	225,000,000
ITRAXX EUROPE CROSSOVER 5Y	5,500,000	20,000,000	45,000,000	55,000,000

Note: Values are displayed in euro.

Further provisional transparency calculations for equity and interest rate derivatives can be found on the ESMA website.

(ii) Market structure: access to trading venues and CCPs

On 7 July 2017, ESMA also provided a number of clarifications on market structure, emphasizing notably that access to trading venues should be non-discriminatory.

In practice, trading venues should refrain from setting minimum requirements in terms of trading activity. Importantly, ESMA lifted the restrictions on the number of counterparties from which quotes can simultaneously be requested in a request-for-quote (RFQ) protocol. Indeed, the market participant initiating the RFQ will have the ability to choose how many counterparties the RFQ is sent to. This paves the way for the wider adoption of what some trading venues refer to as "RFQ-to-All".[60]

With respect to clearing on trading venues, ESMA stated that "members or participants should not be required to be direct clearing members of a CCP". In addition, "for centrally cleared financial instruments, trading venues should not allow participants to require other participants to be enabled before they are allowed to trade with each other."

Regarding systematic internalisers (SI), ESMA clarified that "a system that provides quote streaming and order execution services for multiple SIs should be considered a multilateral system and would be required to seek authorisation as a RM, MTF or OTF." Even if transactions are arranged on one system and subsequently executed on another system, the entity operating those systems has to apply for authorisation as a trading venue.

(iii) Pre-trade transparency waivers

On 28 September 2017, ESMA announced that, in view of the large number of applications received for pre-trade transparency waivers, national regulators and ESMA had reviewed the approval process. Trading venues are required to apply for pre-trade transparency waivers to their national regulator. MiFIR prescribes that national regulators then submit these waivers to ESMA, who in turn will approve the waiver applications by way of opinions.

Considering the large number of waivers, ESMA stated that "it is unlikely to be in a position to issue opinions on a majority of waiver notifications" for bonds and other non-equity instruments. Therefore, national regulators will, subject to certain conditions and pending an ESMA opinion, provisionally grant waivers based on their own assessment. Q&As will be published by ESMA to address key issues and ensure supervisory convergence.

(iv) MiFIR data reporting

ESMA issued further clarifications on technical reporting requirements related to reference data for financial instruments [RTS 23], transaction reporting [RTS 22], and order record keeping [RTS 24] on 7 July 2017.

With respect to pre-trade transparency and record keeping requirements, it is worth noting that "actionable indications of interest are subject to pre-trade transparency requirements, [...] along with current bid and offer prices and the depth of trading interests at those prices." Investment firms and trading venues are required "to maintain records of, amongst others, the relevant data relating to these orders, including actionable indications of interest".

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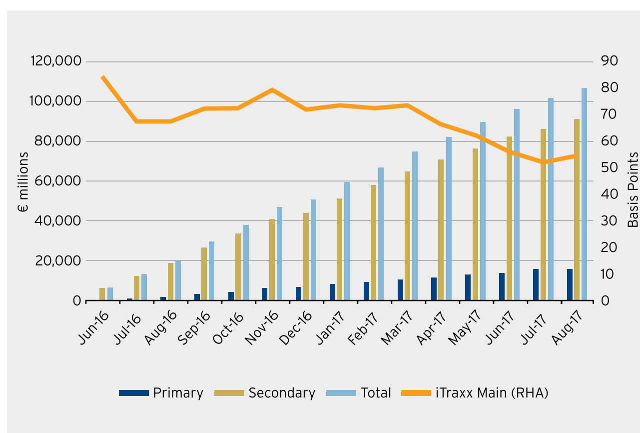
60. "In a request for quote (RFQ) protocol, a trading venue should not impose limits on the number of participants that a firm can request a quote from."

The ECB's Corporate Sector Purchase Programme

In September 2017, the ECB's CSPP entered its 15th month, taking total purchases to over €106 billion, which is around 13% of all eligible bonds. 85% of purchases have been in the secondary market, with 15% primary. While the ECB and participating national central banks (NCBs) have continued to show sensitivity to underlying market liquidity and efficiency, it becomes clear from ICMA's recent study into the state and evolution of the European credit repo market that, as the purchases continue, the effects are increasingly felt in increased repo rate volatility for target issues. Meanwhile credit spreads for eligible bonds remain close to their historical "tights".

CSPP Cumulative Purchases and iTraxx Main



Source: ECB, Bloomberg/Markit[61]

In September, the European Parliament's Committee on Economic and Monetary Affairs (ECON) published a series of papers that investigate the effectiveness, challenges, and future prospects of the CSPP.

A paper by the London School of Economics notes that the purchases to date have been skewed towards bonds issued more recently but with low quality. 24% of holdings are rated BB+ or unrated. It further suggests that while the CSPP provides a technical support bid for the market, market sentiment in general has remained positive, with reduced fears over Brexit and the German elections, and continued inflows for investment grade corporate bond funds. However, it also suggests that while the improvement of financing conditions resulting from the CSPP has mainly helped larger firms to finance themselves, it has had limited impact with respect to SMEs. Furthermore, it argues that the benefits of the CSPP may be felt less in countries where the banking systems remain under pressure, such as Italy and Spain, and where the link between improved financial conditions and higher business investment is weaker. It therefore concludes that, while the CSPP has contributed to the smooth functioning of the transmission mechanism for monetary policy, it is not a substitute for other policy tools, such as the already implemented Targeted Long-Term Refinancing Operations (TLTROs), and the Asset Purchase Programme (APP) more broadly.

A paper by Andrew Hughes Hallett also picks up on this theme, arguing that the CSPP is complementary to, and not an alternative to, QE policies. However, it also argues that corporate bond purchases are a more efficient form of monetary expansion since this bypasses the banking system and also transmissions between extra liquidity and loans for investment, at least in the first round of spending, and does so without the extra debt and deficits that new fiscal spending would entail.

Meanwhile, a paper by the Kiel Institute for the World Economy looks at the effects of the CSPP and suggests that these are very difficult to assess, noting that corporate bonds are not an important refinancing instrument in the euro area, compared to other refinancing instruments, accounting for only 5% of all liabilities of non-financial corporations. It questions whether a further easing of financial conditions can stimulate investment activity, citing evidence that monetary policy is in general less effective in the aftermath of financial crises. It further notes that one important drawback of the CSPP is that it has distributional effects as it favours large firms, that are more likely to use corporate bonds for refinancing, over small and medium sized firms that do not rely on corporate bond markets. It concludes that it is questionable how the CSPP can effectively contribute towards fulfilling the ECB's aims, and that even if the ECB did extend the programme, the effects would likely remain small.

ICMA's Secondary Market Practices Committee (SMPC) remains very focused on the market impacts of the CSPP, and will continue to engage with the ECB, reflecting member concerns and feedback.

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61. iTraxx Main EUR 5 year (generic).

The European single name CDS market

As part of its ongoing work related to corporate bond market efficiency and liquidity, as well as evolving credit market structure, ICMA is collaborating with the International Swaps and Derivatives Association (ISDA) to conduct a study into the state and evolution of the European single name (SN) credit default swap (CDS) market. A liquid and efficient market for hedging and managing credit risk is widely recognised as an important condition for supporting corporate bond market efficiency and liquidity.

The study focuses on a range of issues related to the European SN-CDS market, including current market conditions (tight spreads and low volatility), market participants, capital constraints and other regulatory impacts on market makers, investment and hedging strategies, liquidity and pricing, the development of central clearing, as well as contractual concerns around trigger events and "orphaning".

The study relies on both quantitative and qualitative analysis, and ICMA has conducted a number of interviews with market stakeholders, both sell- and buy-side, as a key part of the research. If member firms who are active in the SN-CDS market would like to participate in the interviews, they should contact Andy Hill or Gabriel Callsen at ICMA.

The report of the study is scheduled for publication in the fourth quarter of 2017.

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High-level data on corporate bond market activity in Europe

To complement ICMA studies and reports and provide an overview of European secondary investment grade corporate bond markets, high-level data from a number of suppliers have been made available on the ICMA website.

From a single point, ICMA members, and other interested market observers, can access historical bond market trading activity, split into Financials and Non-Financials in both EUR and GBP, including:

- Bond trading activity based on executed trades and expressed as "market volume" in EUR and GBP investment grade corporate bonds including the top 10 traded provided by ICE Data Services.
- Evolution of iBoxx and iTraxx indices (IHS Markit), representing investment grade fixed income bonds issued by public or private corporations, and a family of European credit default swap (CDS) indices respectively.
- Inflows and outflows from corporate bond ETFs (Ultumus) domiciled in Europe.

The data will be updated every month.

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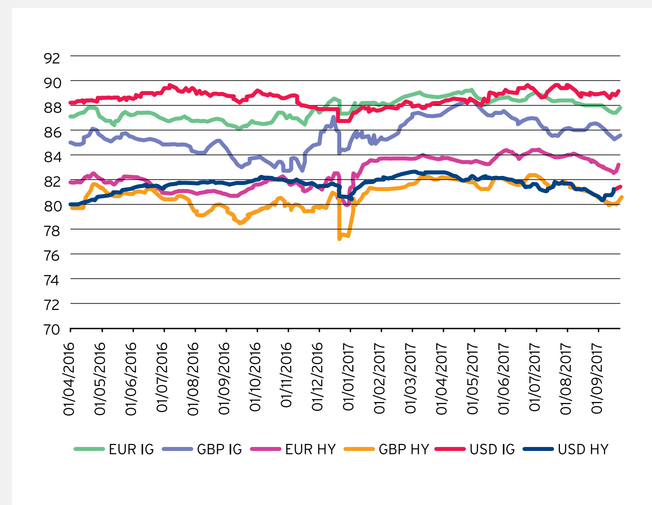
ICE Data Services Corporate Bond Market Liquidity Tracker

September 2017

Liquidity Tracker

ICE Liquidity Trackers are designed to reflect average liquidity across global markets. The ICE Liquidity Trackers 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 Trackers are directly relatable to each other, and therefore, the higher the level of the ICE Liquidity Tracker 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 Trackers 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.

Corporate Bond Liquidity Tracker



Commentary

Perhaps not surprisingly, the revised trackers suggest that IG is more liquid than HY, and that GBP, for the most part, tends to be less liquid than USD and EUR. The trackers also seem to imply that liquidity conditions for both IG and HY for USD and EUR, as well as GBP HY have been relatively stable since the series begins (April 2016), with a somewhat predictable sharp decline around 2016 year-end.

GBP IG liquidity, however, appears to have been more volatile, declining steadily until the middle of November 2016, before recovering sharply to "normalize" with EUR and USD IG liquidity levels by Q2 of 2017. The timing of this decline and recovery seems to correlate closely with the timing of the initiation and cessation of the Bank of England's Corporate Bond Purchase Scheme. The gap to EUR and USD IG, however, widened again in 3Q 2017.

Overall, liquidity levels dropped slightly, reaching similar levels to April 2016 at the beginning of September 2017, before showing signs of improvement towards the end of 3Q 2017.

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Overall, liquidity levels dropped slightly, reaching similar levels to April 2016.

Repo and Collateral Markets

by David Hiscock and Alexander Westphal

European repo and collateral market developments

Bank Recovery and Resolution Directive (BRRD)

On 23 November 2016, the European Commission published a proposal to amend the BRRD, introducing among other things moratoria powers which, *inter alia,* aim to harmonise the use of moratoria tools used by resolution authorities across EU Member States.

In July 2017, the ICMA European Repo and Collateral Council wrote to the applicable senior officials, highlighting its concerns with the proposed moratoria powers, as follows; (i) the negative impact on harmonisation; (ii) the lengthy duration of suspension(s); (iii) the departure from FSB Key Attributes; (iv) the adverse impact on regulatory netting; (v) the adverse interaction with ISDA Resolution Stay Protocol; and (vi) the risk of a run on in-scope institutions.

The ICMA ERCC believes that these concerns provide evidence that there has not been an adequate assessment of the impacts of the proposed moratoria powers; and that this justifies why the proposal should be appropriately revised. In the view of the ICMA ERCC the cumulative impact of these concerns is of such significance that the proposed moratoria powers should be deleted from the Commission's proposed BRRD amendments.

More constructively, the current BRRD framework could be improved by conducting a thorough review of existing moratoria powers across all EU Member States and then using this as a basis for specifically targeted actions to harmonise these, strictly in line with the BRRD and the FSB Key Attributes. Particularly in the context of EU Banking Union, such harmonisation is highly relevant to achieve.

There has not been an adequate assessment of the impacts of the proposed moratoria powers.

MiFID II record keeping and SFTs

In July 2017, ICMA wrote on behalf of its members to ESMA requesting clarification on whether securities financing transactions (SFTs) are considered to be in scope of the MiFID II requirements for order record keeping, as outlined in Article 16 of Directive 2014/65/EU and further specified in Section 8 of Delegated Regulation (EU) 2017/565. ICMA notes that there is already a requirement in force under Article 4.4 of the EU SFTR for counterparties to "keep a record of any SFT that they have concluded, modified or terminated for at least five years following the termination of the transaction".

ICMA further notes that MiFID II/R, in a number of aspects, already takes account of the fact that SFTs are in themselves not outright transactions in transferable securities, but rather they are non-price forming, short-term SFTs (eg SFTs are exempted from MiFID II/R trade reporting obligations, as well as being largely out of scope of transaction reporting and best execution reporting requirements).

Furthermore, there is no specific reference to SFTs in Article 16 of MiFID II, the Delegated Regulation (EU) 2017/580, or the related Q&As, other than with respect to their exemption from transaction reporting under Article 2(5)(a) of RTS 22. It would therefore seem a natural conclusion that while SFTs would be in scope of any SFTR record keeping obligations, they would not be subject to the requirements outlined in MiFID II/R.

Given the significant investment and technological build that would be required by January 2018 for firms to comply with any additional MiFID II/R record keeping requirements with respect to SFTs, ICMA is continuing to seek clarification of any MiFID II/R record keeping requirements for SFTs as soon as possible.

Secured benchmarks/indices

As reported in this section of Issue 46 of the ICMA Quarterly Report, on 15 June, an important market consultation was published by the European Money Markets Institute (EMMI), in relation to its ongoing work on a new transaction-based repo index for euro-denominated debt. On 29 August, EMMI released feedback on this consultation. EMMI reported that: "Overall, the feedback received is supportive of EMMI's plans for the new index and acknowledges the Institute's commitment to initiate the debate regarding the search for eligible and adequate alternative reference rates in the Eurozone. EMMI stands ready to be an active part of this process and encourages market participants to identify for which products the new repo index could be used."

Other recent developments relating to financial benchmarks are reported in the International Regulatory Digest, further on in this ICMA Quarterly Report.

Asset segregation and custody services

On 20 July, ESMA published an opinion to the European Commission, the Council and the Parliament (EU institutions), setting out suggestions to the EU institutions for possible clarifications of the legislative provisions, under both AIFMD and UCITS, relating to (i) the asset segregation requirements in case of delegation of safe-keeping duties by the appointed depositary of a fund (UCITS or AIF); and (ii) the application of depositary delegation rules to CSDs. This opinion is the final step of the work on these topics which began with a 2014 consultation paper, which was then followed by a 2016 call for evidence, to which the ICMA ERCC responded.

Money market funds

As reported in this section of Issue 46 of the ICMA Quarterly Report, on 24 May, ESMA launched a consultation inviting responses to specific questions on draft technical advice, implementing technical standards and guidelines under the EU MMF Regulation (MMFR). On 8 August, ESMA announced that it had published the duly submitted responses.

Trade association responses, such as those of IMMFA, EFAMA and ICI Global, as well as those of some individual industry respondents, include a number of points relating specifically to the MMFs' repo market activities. In general, these seek less prescriptive rules, such that MMFs would be able to more flexibly and practically use repo markets within the context of their overall risk management frameworks.

Survey on euro-denominated securities financing

On 10 July, the ECB published the results of the June 2017 survey on credit terms and conditions in euro-denominated securities financing and OTC derivatives markets (SESFOD), which showed little overall change in credit terms for secured funding. Regarding the provision of finance collateralised by euro-denominated securities, respondents reported a decrease in financing rates/spreads for many collateral types, particularly government bonds; a further increase in the use of CCPs for SFTs; and increased demand both for funding collateralised by equities and for longer term funding collateralised by domestic government bonds. They also reported a further deterioration in the liquidity and functioning of the market for domestic government bonds; while for other asset classes covered by the survey only small changes in liquidity and functioning were reported for the March to May 2017 reference period, compared with the more significant deteriorations reported over the past two years.

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Autumn 2017 ICMA ERCC General Meeting

The ICMA ERCC was established by ICMA in 1999 to provide a forum for practitioners in cross-border repo to discuss ways of enhancing the functioning of this pivotal financial market and to consult with market users, infrastructure providers, policy makers and regulators. The ERCC hosts two General Meetings each year.

The next ERCC General Meeting, which is being held in Brussels on 14 November, will be used as an opportunity to deepen the exchange of ideas between the market, the public sector and academia at this critical time in the post-crisis programme of regulatory reform. Between keynote addresses from the IMF – Mahmood Pradhan (Deputy Director, European Department) and the ECB – Benoît Cœuré (Member of the Executive Board), there will be two panel discussions, involving industry representatives, regulators and academics. These panel discussions will address general market conditions and operational challenges affecting the effectiveness of repo markets and their macro-financial implications on the path towards greater financial integration across Europe, while making clear the valuable and important role of the repo market at the heart of a collateralised financial market system.

This event is hosted in conjunction with the Euroclear Collateral Conference 2017. Admission is open to all ICMA members and to interested financial market participants, free of charge; however, registration in advance is essential.

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SFT Regulation

The SFT Regulation (SFTR) itself entered into force in January 2016, but the technical standards which set out the details of the reporting regime are still under review by the European Commission. It is currently expected that these should be approved towards the end of this year, which would mean that the reporting regime would go live around mid-2019 for most market participants, including banks. In the meantime, the ERCC SFTR Task Force continues to prepare for the upcoming implementation of the extensive reporting rules.

Among the biggest SFTR implementation challenges will be the required reconciliation of reports. Given the double-sided nature of SFTR reporting, both sides of the report will have to be matched, within and across trade repositories (TRs), where necessary. To address this challenge early and reduce the likely operational burden resulting from unmatched trade reports, on 2 June the ERCC SFTR Task Force launched a bilateral SFTR reconciliation exercise for repo and buy/sell-back trades. The feedback from this exercise is hoped to provide a good basis for further, more detailed work on the most problematic reporting fields. In addition, the group is also trying to get more clarity on the rules set out in ESMA's draft standards published by ESMA in March this year. Several outstanding questions have already been identified and raised to authorities and others are likely to follow.

Another important aspect of the implementation is cross-industry collaboration. The ERCC has been working closely with other industry associations, particularly ISLA, to address SFTR challenges in common. In addition, there is an important role to play for service providers in the SFTR space. To deepen discussions with vendors, it is planned to set up over the coming months a series of bilateral meetings with the relevant firms. The objective will be to help ERCC member firms to develop a better understanding of emerging solutions, but also to support vendors to shape their products in accordance with market needs and to encourage discussion between vendors to allow for interoperable solutions.

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Results of pilot survey of repo markets in Asia-Pacific

ICMA's European Repo and Collateral Council (ERCC) and ASIFMA's Secured Funding Markets Committee commissioned a pilot survey of the Asia-Pacific repo markets. It uses similar methodology to the long-established ICMA ERCC European repo market survey, which reports the value of repos and reverse repos outstanding in the market at close of a chosen business day, in this case 7 December 2016.

Asian repo has been defined, for the purposes of the survey, as repo (i) involving at least one party

dealing from a location in Asia in any currency or against any collateral or (ii) between parties located anywhere but in an Asian currency and/or against collateral issued in Asia.

The main findings of the survey were:

- Most collateral was reversed in by repo desks located in Japan from counterparties in the domestic market and mainly repo-ed out cross-border to counterparties outside Asia.
- Collateral in the form of sovereign securities formed a larger share of the Asian market than the European market (at least as measured in the surveys).
- The largest share of collateral was Japanese, but there was also a significant amount of US collateral.
- The main currency traded in the Asia-Pacific repo market was Japanese yen, of which the reporting banks were net lenders. There was some cross-currency repo between US dollars and Japanese collateral.
- Most transactions were executed directly on the telephone and electronic messaging systems. Voice-brokers were heavily involved in reverse repos from domestic counterparties. There was very little electronic trading.

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Asset Management

by Patrik Karlsson and Bogdan Pop

MiFID II/R implementation: research unbundling

It is now less than three months until the new MiFID II unbundling rules come into effect. Several large asset managers have announced their position in recent months on how to pay for research, establishing a market trend towards firms absorbing the costs and not passing them directly on to clients by using a research payment account (RPA). Despite this trend, there are still many asset managers who have not yet decided or are still negotiating with their clients about the possible outcome.

In the ESMA Investor Protection Q&A, Question 8 states that an exception to macroeconomic research being considered "research" is where a provider makes macroeconomic-related material openly available at the same time to any investment firms wishing to receive it or to the general public, for example on a website. Material made available in this way could be justified as a minor non-monetary benefit – representing "information … relating to a financial instrument or investment service" that is "generic in nature" under Article 12(3)(a) of the Delegated Directive. While this would not capture all FICC research (particularly where research recommends a specific investment strategy), it could allow more generic FICC papers to be shared freely.

There have been numerous press articles on the likelihood of one or more broker dealers publishing their FICC research in this way, but few confirmed cases. This is an evolving area of the research unbundling implementation process which AMIC will continue to monitor on behalf of members. More details on the ESMA Q&A can be found in an AMIC briefing. The FCA has recently commented that there is a settled picture in terms of policy expectations on the MiFID II research rules, with ESMA not expected to produce any further Q&A or guidance materials on this topic.

Once the unbundling rules come into force, it is widely expected that buy-side participants will consume less external research and may attempt to offset this by increasing in-house research capabilities or relying more on research made available for free by various research providers, as described above.

Research providers will eventually need to adjust to meet this reduced demand. This has raised concerns about the potential for reduced coverage of smaller issuers which could in turn lead to a change in investor behaviour towards debt issues. In the long term, however, it is possible that specialist research providers could fill the gap and increase coverage of smaller issuers, as the value of research becomes more established.

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Leverage in investment funds

On 17 July 2017, AMIC and EFAMA published a *Joint Report on the Use of Leverage in Investment Funds*. This is the second joint paper issued with EFAMA after last year's *Report on Liquidity Risk in Investment Funds*.

The leverage paper analyses how leverage is used, how the European legislative framework addresses leverage, and how the related risks are addressed from a technical perspective. To contribute to recent debates launched by regulators and supervisors, it also looks at the updates and improvements that could be proposed to ensure that the European regulation remains a cutting-edge framework at global level.

AMIC and EFAMA explore recommendations and proposals to improve monitoring and analysis of leverage risk.

The paper sets out how and why leverage is used in investment funds. The paper then assesses the main technical tools used to measure leverage: the commitment method, the gross method, as well as a frequently used risk-based measure, the Value at Risk (VaR) method. The paper examines the detailed, specific requirements in both the UCITS and the AIFMD legislative frameworks on leverage. The paper also addresses some of the concerns by regulators regarding risks related to the use of leverage, including counterparty and fire sale risk.

Finally, AMIC and EFAMA explore recommendations and proposals to improve monitoring and analysis of leverage risk:

- There is no single measure that can capture all the risks in nature, size and characteristics associated with a fund's underlying assets. A matrix of different measures is the only way to allow a meaningful representation of a fund's exposures. The existing regulatory standards at EU level can be the basis for developing leverage and risk measurements through such a matrix.
- Further streamlining of global calculation methodologies for leverage and risk can be envisaged. For that, we recommend that regulators should use the existing EU framework as a reference point for a globally consistent regime: European regulators have been able to rely on this framework to assess levels of leverage in funds since the financial crisis and take appropriate supervisory action. The Net/Commitment Approach could become a "Standard Method", complemented where appropriate by the VaR Approach as an "Advanced Method", which, in combination with stress testing, can assess potential downside risks. The gross method can be an additional model to complement this matrix of methodologies only to the extent that it is used as a source of information related to the overall synthetic leverage footprint of a fund. Adjustments and improvements of these methods, particularly by increasing the instruments covered in the 2010 CESR Guidelines, based on the best practices at EU level, could be envisaged if properly justified.
- A key measure of progress for regulators in better assessing the overall risks related to funds in Europe and at global level would be to improve data sharing among them. This would allow identification and monitoring of key areas of risks for macroprudential policy reasons. In that context, there is merit in streamlining reporting requirements at EU level.

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Fund liquidity risk management

On 18 September 2017, AMIC responded to IOSCO's consultations on (1) *CIS Liquidity Risk Management Recommendations* and (2) *Open-ended Fund Liquidity and Risk Management – Good Practices and Issues for Consideration*.

In its response to the *CIS Liquidity Risk Management Recommendations*, AMIC broadly agrees with the suggested amendments to IOSCO's 2013 liquidity risk management recommendations. However, AMIC suggests some amendments to the recommendations to bring them in line with current market practice. Furthermore, AMIC counsels caution on stress tests, which can be misleading, particularly at a systemic level.

AMIC also welcomes the consultation report on *Open-ended Fund Liquidity and Risk Management – Good Practices and Issues for Consideration*, which helpfully references AMIC's 2016 joint report with EFAMA on *Liquidity Risk Management*.

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Central Bank of Ireland: ETFs

The Central Bank of Ireland (CBI) issued a consultation in the form of a discussion paper on ETFs on 15 May 2017. AMIC responded to this consultation by the deadline of 11 August 2017. The Central Bank of Ireland (CBI) discussion paper on ETFs examined all relevant aspects of ETFs and their regulation. It reviewed a very significant amount of academic literature available on the effect of ETFs (albeit much of it only from the US) and asked several questions about key topics of ETF functioning.

The paper highlighted several overarching themes of ETF regulation: investor expectation, liquidity, and increasing

popularity of ETFs. AMIC decided to focus on only certain topics of the discussion paper, relevant to previous AMIC activities: the potential for systemic risks in ETFs and the impact of ETFs on corporate bond liquidity. Broadly, AMIC stressed that there are no unique risks to an ETF which are not already addressed by the UCITS and MiFID frameworks.

With regard to systemic risk in ETFs:

- AMIC stressed that, although frequently cited in the text, the ESMA 2012 ETF Guidelines were not sufficiently taken into account by the CBI in their analysis and questions. Many of the issues that are raised by academic literature in the discussion paper are already addressed by the Guidelines and do not need further policy measures.
- Furthermore, AMIC stressed that the Guidelines focused on UCITS ETFs. It is therefore important to distinguish between UCITS ETFs and other types of exchange traded products such as ETN, ETIs and ETCs which, although exchange traded, have a different structure and are subject to different regulatory requirements.
- In general, AMIC members' feedback showed support for the current EU regulatory framework, and the 2012 Guidelines in particular, to address specific risk factors, like group concentration of activities for instance.
- AMIC did not support regulating the number of counterparties for ETFs, but supported disclosing counterparty arrangements to investors.
- AMIC also supported the existing 2012 ESMA Guidelines on collateral quality, which it regarded as sufficient. AMIC warned CBI against introducing a strict correlation requirement between synthetic ETFs and its collateral received. AMIC also noted that requiring an unfunded model to purchase securities, or a funded model to receive collateral that is correlated to the underlying index, may not be practical in many scenarios. In addition, it may be more practical and efficient for certain synthetic ETFs to hold or receive securities or collateral that have a lower liquidity risk.

With regard to market liquidity:

- AMIC welcomed the thorough aggregation and analysis of academic literature into the effect of ETFs on market liquidity conditions in Section IV. AMIC agrees with the CBI that there is not necessarily any need to regulate any potential long-term negative effect on liquidity.
- Regarding liquidity risk management for ETF structures, as the funds are UCITS funds, the same liquidity risk management tools and practices that are used by vanilla UCITS funds are also available to be used by ETF funds. The AMIC/EFAMA report on *Investment Funds Liquidity Risk Management* contains details about these tools, although not all tools will be relevant for ETFs. ETFs will have additional liquidity risk management practices, befitting their structural differences with funds which are not traded on exchange.
- Where ETFs are tracking indices of underlying stocks which are not sufficiently liquid to match the intra-day liquidity on the secondary market which the ETF offers, AMIC reminded CBI that that there may be significant secondary market activity but very little primary market activity. AMIC also stressed the significant pre-launch analysis of liquidity conditions that ETF providers undertake.

Regarding the CBI's conclusion that in the long-term ETFs may have a detrimental effect on price discovery and volatility, AMIC responded that this hypothesis should be tested more, especially in Europe.

AMIC will continue monitoring developments and any follow-up the CBI may undertake, which could lead to more ETF-specific activity on the European level.

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AMIC Council

The AMIC Council holds two plenary sessions annually, both to advise the Executive Committee of AMIC on priorities and to discuss current issues at the biannual conferences – organised in the spring in a continental European city and in the autumn in London. The last AMIC Council was held in Frankfurt on 23 March 2017, hosted by Allianz GI. The next Council will be held in London on Wednesday 8 November, hosted by Schroders. These meetings also provide excellent networking opportunities for the AMIC community.

The 2017 autumn AMIC Council conference will be held on 8 November at Schroders' offices in London. Huw van Steenis, Global Head of Strategy at Schroders, will feature as a keynote speaker. Panel discussions will include the future of the asset management industry, systemic risk and research unbundling in MiFID II. More details, including how to register, are available here.

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European infrastructure finance

By Katie Kelly

A new report, *European Infrastructure Finance: a Stock-take*, has been released by the AFME ICMA Infrastructure Working Group. The report is a review of the state of infrastructure financing, investment and related initiatives in Europe, and an assessment of how to further advance and encourage private sector finance for infrastructure projects.

There can be little doubt that more and better infrastructure is required globally. According to a study conducted in June 2016 by McKinsey, $3.3 trillion needs to be invested each year globally to 2030 to support currently expected rates of growth (with the majority being required in emerging economies) – quite an increase over current investment levels of $2.5 trillion per year.

Banks are of course big financiers, but meanwhile an alternative yet complementary source of liquidity has been emerging. It is estimated in the same McKinsey report that institutional investors (such as pension funds, insurance companies and sovereign wealth funds) have $80 trillion in assets that could partially support infrastructure projects, and the number of institutional investors in the infrastructure asset class has increased by over 116% between 2013 and 2016. Further, a number of large institutional investors are developing dedicated infrastructure teams, all of which indicates the availability of capital and the continued potential growth prospects in this asset class.

Institutional investors typically seek infrastructure assets offering long-term stable returns that match their liabilities, and generate sufficient revenue to provide them with maximised returns over the life of the project. In particular, project finance transactions often provide good diversification within an investor's portfolio given the relative lack of correlation to the broader economy.

Notwithstanding this, according to other studies, 63% of institutional investors are below their target allocation to infrastructure, the reasons for which may include investor concerns regarding the pricing of infrastructure assets eating into the eventual returns, and the availability of assets for deals. But the fundamental bottleneck overwhelmingly cited for under-investment in infrastructure over a number of years has been the supply of investible projects.

So how best to boost the pipeline of projects and harness this source of finance to best match the infrastructure financing deficit? Therein lies the challenge that the report seeks to address. The report highlights measures which, together with a mix of financial instruments and innovative financing solutions, could help to generate a positive environment to boost private sector infrastructure investment, including:

- understanding, structuring and allocating risk, including country-specific risk;
- the importance of coherent and trusted legal frameworks to ensure long-term regulatory and political stability, and the equal treatment of foreign, local and institutional investors;
- developing expertise and standardisation of best practice;
- more and better-quality disclosure of information on infrastructure projects and on ongoing infrastructure debt performance; and
- a review of regulation to ensure that there are no disincentives for investing in infrastructure as against other asset classes.

Much remains to be done, and ICMA remains committed to exploring the forces required to boost infrastructure finance, to encourage and facilitate the debate among its members and to help drive forward the changes required.

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Green and Social Bond Markets

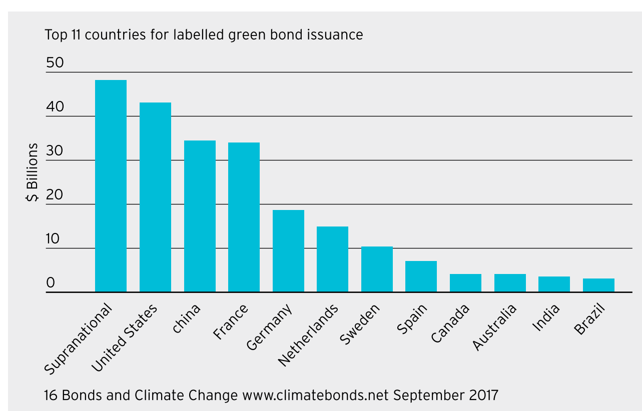
by Nicholas Pfaff, Valérie Guillaumin and Peter Munro

Green, social and sustainable bond market developments

Market growth

With issuance in the first nine months of 2017 well over $80 billion, surpassing the total for the whole of 2016, the market continues to grow significantly. Volumes have been buoyant across asset classes, with the private sector leading in terms of issuance volume in the past 18 months. In terms of the geographic spread of the stock of outstanding bonds aligned with the GBP, the Supranationals lead (approaching $50 billion), closely followed by the US (close to $45 billion), China and France (both approaching $35 billion).

Figure 1: Stock of green bonds



16 Bonds and Climate Change www.climatebonds.net September 2017

Tenors have been lengthening, led by EUR with an average around 12 years and USD around 10 years. Across all currencies the average tenor of the stock is closer to 8 years.

EU HLEG on Sustainable Finance

ICMA and the GBP Executive Committee responded to the questionnaire of EU's High Level Expert Group (HLEG) on Sustainable Finance following its interim report. In summary, our response focused on emphasizing that:

- a future EU taxonomy on sustainable assets should focus on assets and projects rather than on financial products, as the former will serve as the basis for further development of sustainable financial products by the market itself;
- as recommended in the interim report, the EU should base any potential future European green bond standard on the definitions and best practice developed by the Green Bond Principles;
- the Commission considers the potential of social bonds to mobilise capital for the social dimensions of sustainable development.

Global Green Finance Council

The Global Green Finance Council (GGFC), for which ICMA provides the Secretariat, held its third meeting on 17 July 2017 in Brussels hosted by the European Banking Federation. A key item on the agenda was the interim report of the European Commission's High-Level Expert Group (HLEG) on sustainable finance, which the GGFC welcomed through a common press statement. The GGFC said in particular that: "Practical proposals such as for a common classification for sustainable projects, support for green finance guidelines and a disclosure framework that promotes harmonisation of metrics are positive developments".

As a reminder, the GGFC assembles mainly financial sector trade associations with the aim to coordinate and cross-fertilize green finance initiatives, and to pursue an open

and constructive dialogue on green policy issues with the official sector. The members of the GGFC currently include AFME (Association of Financial Markets in Europe), EBF (European Banking Federation), EMF-ECBC (European Mortgage Federation - European Covered Bond Council), GFMA (Global Financial Markets Association), ICMA, IIF (International Institute of Finance), LMA (Loan Market Association), and WFE (World Federation of Exchanges). Participating observers are CERES, EFAMA (European Fund and Asset Management Association), EFR (European Financial Services Roundtable), and Insurance Europe.

Award for Social Bond Principles

The release of ICMA's Social Bond Principles was voted "most important innovation" in 2017 In the annual Global Capital poll on sustainable capital market themes. This underlines both the quality and depth of the output from the Social Bonds Working Group – coordinated by Crédit Agricole CIB and IFC and involving no less than 32 institutions, and also the development of the social bond market.

Accepting the award from John Hay,Global Capital, IFC's Elena Panomarenko, Joint Leader (with CACIB) of the Social Bond Principles Working Group; René Karsenti, President of ICMA and also Chairman of IFFIm, an early pioneer of social bond issuance; Hans Biemans from ING, a member of the SBP Working Group; and Allan Malvar, MD and Member of ICMA's Executive Committee.

Translations of the international GBP/SBP/SBG guidelines published

Translation of the international GBP/SBP/SBG guidelines was arranged in a matter of weeks thanks to generous voluntary input from GBP and SBP members and observers, illustrating their diversity and commitment to the green bond market. All three sets of documentation (Green Bond Principles/Social Bond Principles/Sustainability Bond Guidelines) and a list of topical Questions and Answers on Green, Social and Sustainability Bonds are in the process of being made available in twenty languages, including existing English versions, to ease local adoption, as the global market expands. Access to those translations already rolled out is freely available from the ICMA website.

The documents are, or will be available soon, in the following languages: Bulgarian, Chinese, Danish, Dutch, English, Finnish, French, German, Hausa, Hindi, Italian, Japanese, Norwegian, Polish, Portuguese, Romanian, Russian, Spanish, Swedish, Turkish.

Forthcoming Tokyo event on Green and Social Bonds

A conference on *Developments in the Green and Social Bond Markets – the Asian Perspective* will take place in Tokyo on 2 November, organised by ICMA with the support of the Japan Securities Dealers Association (JSDA). This conference will build on the sharp growth in Asian green bond activity, the recent launch of guidelines by the Japanese Ministry of Environment, as well as pioneering social bond issuance and increased investment in such products in the region. Asian green bond issuance increased roughly tenfold in 2016 to approximately $28 billion, led by China, and prominent Asian investors have announced plans to invest in green bonds. Asian issuers were amongst the first to apply Social Bond Guidance issued by ICMA in 2016. Also, an ecosystem of green and social bond expertise and services has developed in the region.

Speakers will include senior representatives from regulators and supervisory authorities, including the Japanese Ministry of Environment, China's Green Finance Committee and the ASEAN Capital Markets Forum; other leading public-sector players, including the Governor of Tokyo and the OECD; as well as a wide array of prominent issuers, intermediaries, investors and service providers. The event is being made possible by generous sponsorship from the JSDA and an array of other private sector sponsors. Registrations are open here.

Working Groups

Thanks to support from the GBP ExCom and wider GBP community, the range of working groups is expanding for the 2017-2018 cycle. There will be a revival of the group on External Reviews and addition of a group working on Green Bond Labels and Lists.

The range of groups is listed below. Should you wish to get involved, please contact the Secretariat for further information (greenbonds@icmagroup.org or socialbonds@icmagroup.org). In order to keep the groups relevant and manageable in terms of size, the involvement of new participants is subject to adequate contributions of expertise and the operational capacity of the group.

Working Groups of the GBP & SBP Executive Committee

• Green Projects Eligibility • Social Bonds • Impact Reporting • Index & Database	• New Markets • External Reviews • Green Bond Labels and lists

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IFFIm's impact on SRI reflected in new Social Bond Principles

By René Karsenti

When the International Finance Facility for Immunisation (IFFIm) was established in 2006, it pioneered a unique form of investments. Its Vaccine Bonds bring donors and investors together to support efforts to save children's lives through vaccine programmes in the world's poorest countries.

Today, demand among investors for socially responsible products is higher than ever. Responding to this trend, the International Capital Market Association in 2017 issued guidelines for socially responsible investments (SRI). The result: ICMA's Social Bond Principles (SBP).

ICMA's decision to think through and define best practices in this area is an encouraging sign of the continued evolution and maturation of socially responsible investing. This is a big and valuable step ahead for the field that IFFIm has been part of since 2006.

Social bonds are any type of bond instrument where the proceeds will be exclusively applied to finance or refinance eligible social projects that are aligned with the four core components of the SBP. The SBP are voluntary ICMA guidelines that promote transparency and integrity for any sort of social bond. Following in the footsteps of the Green Bond Principles, the SBP offer guidance for issuers, investors, and underwriters.

IFFIm's Vaccine Bonds, one of the world's most impactful social bonds, meet all four Social Bond Principles:

1. *Use of proceeds:* The new SBP specify that "all designated Social Projects should provide clear social benefits, which will be assessed and, where feasible, quantified by the issuer." In IFFIm's case, all proceeds go to support Gavi's mission to improve access to life-saving vaccines for the world's most vulnerable children. In fact, IFFIm was designed to be – and remains – completely dedicated to that mission.

2. *Process for project evaluation and selection:* The SBP also "encourage a high level of transparency and recommend that an issuer's process for project evaluation and selection be supplemented by an external review." This guidance has always been at the core of IFFIm's operations. Gavi's potential vaccine investments are evaluated by an expert Independent Review Committee (IRC), and IFFIm funds vaccine programmes selected through the IRC evaluation and approved by Gavi's Board.

3. *Management of proceeds:* The SBP prescribe that "the issuer should make known to investors the intended types of temporary placement for the balance of unallocated proceeds" and "recommend that an issuer's management of proceeds be supplemented by the use of an auditor, or other third party, to verify the internal tracking method and the allocation of funds from the Social Bond proceeds." All IFFIm proceeds are allocated to support Gavi's vaccine purchase and health system strengthening programmes. Gavi manages the allocation, disbursement and tracking of IFFIm's proceeds in a transparent manner, in accordance with its programme funding policies. Gavi programmes, including those funded by IFFIm, are regularly evaluated to ensure that Gavi support has been used as intended.

4. *Reporting:* Finally, ICMA calls on social bond issuers to "make, and keep, readily available up to date information on the use of proceeds to be renewed annually until full allocation, and as necessary thereafter in the event of material developments." The World Bank, IFFIm's Treasury Manager, monitors its investments and reports outcomes quarterly to its investors and other stakeholders. IFFIm also regularly reports to donors its performance outcomes against impact indicators.

IFFIm offers investors a unique opportunity to combine an attractive financial investment with an exceptional social purpose generating a major positive impact on society. Its compliance with the new Social Bond Principles gives investors the confidence it will remain true to that mission.

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For further information
www.iffim.org
www.gavi.org

IFC's social bonds: doing good and doing well through the bond markets

By Denise Odaro

Imagine a different kind of business – companies that do business with people who live at the "base of the economic pyramid" (BOP) recognizing that the 4.5 billion people at the BOP spend small amounts individually, but in aggregate they spend $5 trillion a year. Imagine a business that considers gender equality as not only a social and moral imperative, but also an economic need recognizing that the credit gap for women-owned SMEs is estimated at close to $300 billion. These are the types of businesses which are supported by IFC's Social Bond Program.

Um Sreytouch, lives in a village on the Tonle Sap River in Cambodia where skilled metal artisans flatten pieces of silver and copper into pots, plates, bracelets, and other ornaments. Visitors traveling up the river from Phnom Penh to Angkor Wat stop at the village and buy artisan goods from Sreytouch, a 49-year-old widowed mother of four who makes and sells handicrafts in her own shop and supplies her products wholesale to souvenir shops all across Cambodia. Sreytouch started out with a micro-loan of $500 from IFC partner ACLEDA Bank, Cambodia's largest bank, with a branch network in all provinces and municipalities. After purchasing her first silver and copper, and learning the handicrafts business over six years, she obtained another ACLEDA Bank loan for $25,000 to expand her workshop, hire more workers, and buy more raw materials which enabled her business flourish. With proceeds from the Social Bond Program, IFC provided a syndicated loan of $240 million to ACLEDA Bank Plc to boost lending to SMEs, of which at least half will support women-owned enterprises. With this funding, ACLEDA Bank Plc aims to increase its outstanding portfolio of loans to women-owned enterprises to more than $1.5 billion by 2019.

IFC's Social Bond Program is aligned with ICMA's Social Bond Principles. The bonds' proceeds are ringfenced for disbursement to inclusive businesses and financial intermediaries with a condition of on-lending to women entrepreneurs. Inclusive business models are those which integrate low-income consumers, suppliers, retailers or distributors in their core business operations, on a commercially viable basis. The program is complemented with an annual impact report. IFC started to issue themed bonds in 2010 with the launch of its Green Bond Program. In 2013, IFC expanded its thematic products to include the Banking on Women (BOW) Bond Program, the first bond program of its kind focused on creating opportunities for women entrepreneurs in emerging markets. In October 2014, IFC's Inclusive Business Bond Program was created as the first debt offering to exclusively support businesses which include low-income communities into their value chains. The BOW and Inclusive Business Bonds were sold to retail investors and in private placement format to institutional investors.

IFC's Social Bond Program was created by merging the BOW and Inclusive Business Bond Programs. Through the new program, IFC has the scope to issue benchmark sized bonds along with private placements and targeted retail issues tailored to investor preference. This expands access to the product for investors sensitive to issue size. IFC's inaugural social bond offering, a $500 million, three-year bond paying a coupon of 1.75 percent and issued IFC in March 2017, was the first ever labelled social bond in the US dollar public market. The transaction was oversubscribed and bought by more than forty institutional investors across diverse regions. The transaction enlarged IFC's investor base with the order book comprising around 20 percent new investors.

Investor appetite for ESG bonds is on the rise, emulating the trend in the equities market where ESG has played more of a historical role. Social bonds, although nascent a product, could bring the much-needed depth and growth to the ESG bond universe in several ways:

Liquidity: Use-of-proceeds social bonds are structured similarly to green bonds and could potentially fit in the same bond portfolios because the risk remains at the issuer level. Issuing liquid benchmarks under the social bond label will take the product more mainstream as well as grow the ESG bond product through diversity by issuer and product type.

Issuer diversity: The wide use-of-proceeds for social bonds means that more issuers can identify suitable projects to enable a sustainable pipeline that would form the basis of an issuance program.

Standardization: Issuing under the social bond label should mean that the bond meets the characteristics outlined in Social Bond Principles and that the issuer intends to meet the standards set therein.

While the market is currently in infancy, as investors continue to incorporate ESG factors into their portfolioconstruction, the market is only poised for growth.

Esohe Denise Odaro *is Head of Investor Relations, IFC.*

International Regulatory Digest

by David Hiscock, Alexander Westphal and Gabriel Callsen

G20 financial regulatory reforms

On 6 July 2017, the FSB published two guidance documents, to assist authorities in implementing the FSB's TLAC standard and facilitating the continued access to critical financial market infrastructure services in resolution:

Guiding Principles on the Internal Total Loss-Absorbing Capacity of G-SIBs supports the implementation of the internal TLAC requirement, and provides guidance on the size and composition of the internal TLAC requirement, cooperation and coordination between home and host authorities and the trigger mechanism for internal TLAC.

Guidance on Continuity of Access to Financial Market Infrastructures (FMIs) for a Firm in Resolution sets out arrangements and safeguards to facilitate continuity of access to FMIs for a firm in resolution that apply at the level of the providers of FMI services, at the level of FMI participants and at the level of the relevant resolution and FMI authorities. Both of these guides were issued for public consultation in December 2016 and have been revised in light of the comments received.

At the same time, the FSB also published its sixth report on the implementation of post-crisis resolution reforms, *Ten Years On – Taking Stock of Post-Crisis Resolution Reforms*. This reports the findings from the resolvability assessment processes for G-SIBs and G-SIIs and sets out the further actions necessary to fully implement the Key Attributes and ensure that all G-SIFIs are resolvable. The focus going forward will be on the comprehensive and consistent implementation of agreed resolution policies and on the evaluation of the effects of resolution reforms.

The twelfth G20 Summit at the level of the Heads of State and Government took place, in Hamburg on 7-8 July. Following the Summit, a G20 Leaders' Declaration, *Shaping an Interconnected World*, was issued, which presents a series of agreed points organised under the headings of (i) sharing the benefits of globalisation; (ii) building resilience; (iii) improving sustainable livelihoods; and (iv) assuming responsibility.

Concerning the ongoing process of financial regulatory reform, under the second of these headings there is a paragraph entitled "Resilient Global Financial System". Reporting this in a bullet point format, it says:

An open and resilient financial system, grounded in agreed international standards, is crucial to supporting sustainable growth.

- We remain committed to the finalisation and timely, full and consistent implementation of the agreed G20 financial sector reform agenda.
- We will work to finalise the Basel III framework without further significantly increasing overall capital requirements across the banking sector, while promoting a level playing field.
- We will continue to closely monitor

and, if necessary, address emerging risks and vulnerabilities in the financial system.

- We emphasise the considerable progress made towards transforming shadow banking into resilient market-based finance since the financial crisis and welcome the FSB assessment of the monitoring and policy tools available to address risks from shadow banking.
- We support the FSB's work to analyse the effects of financial regulatory reforms and the structured framework for post-implementation evaluation.
- Acknowledging that malicious use of ICT could endanger financial stability, we welcome the progress of the FSB's work and look forward to a stock-take report in October 2017.

Amongst the various supporting papers published by the G20 there is an, 8 July, G20 Hamburg Action Plan. Section 4 of this is headed "Financial Sector Regulation and Development" and includes segments on (i) implementing and developing the FSB agenda; (ii) digital finance; (iii) cyber security; and (iv) financial inclusion and literacy.

Looking further ahead, on 1 December 2017, Argentina will take over the G20 Presidency and organise the G20 summit in 2018.

On 2 August, the Financial Stability Institute (FSI) launched a new publication series, *FSI Insights on Policy Implementation*, to contribute to international discussions on a range of policy issues and implementation challenges faced by financial sector authorities. The first two papers in this series focus on proportionality and on cyber-risk.

The paper on proportionality explores the issue of how best to tailor regulatory requirements for different types of banks by comparing the approaches followed in six significant jurisdictions. It shows the range of approaches in terms of criteria and the thresholds used to differentiate banks, and also in terms of the regulatory standards that are subject to a proportional implementation. The paper notes that implementation of the proportionality strategy should respect prudential objectives and consider implications for the competitive environment.

The paper on cyber-risk explores regulatory and supervisory initiatives in some leading jurisdictions. While there may be different views on the need to specifically regulate cyber-risk or how prescriptive these regulations should be, the supervisory approaches to assessing banks' cyber-risk vulnerability and resilience seem to be converging towards a "threat-informed" or "intelligence-led" framework. The paper also offers some high-level policy considerations for banking supervisory authorities contemplating or planning to introduce or enhance cyber-risk regulation and supervision for banks.

On 5 September, the BCBS and the IFRS Foundation announced a new cooperation agreement to foster long-term financial stability, enhance market discipline and further develop sharing of information (such arrangements already exist between the IFRS Foundation and a number of organisations, including, for example, IOSCO). The new agreement, in the form of an MoU, formalises the mutual interaction and strengthens the existing relationship between the BCBS and the IFRS Foundation at the strategic and working level, focusing on the development of IFRS Standards, the interaction between IFRS Standards and the BCBS Framework and the manner in which they are applied in practice by financial institutions across the world.

The relationship between the BCBS and the IFRS Foundation is a long-standing one – the BCBS has been an observer at the Foundation's Monitoring Board since the Monitoring Board's creation and has been continuously represented at the IFRS Advisory Council; and the BCBS's Accounting Experts Group regularly interacts with representatives of the Foundation's standard-setting board, the IASB. Although the relationship between the BCBS and the IFRS Foundation pre-exists its formal recognition, there is perceived value in agreeing an MoU via a public statement endorsed by both organisations. This MoU is not intended to change the relationship between the two bodies, but rather

We will continue to closely monitor and, if necessary, address emerging risks and vulnerabilities in the financial system.

seeks to formalise the existing relationship, and thereby strengthen it.

Taking place on 18-19 September at the BIS, in Basel, the Financial Stability Institute's (FSI's) two-day conference on cross-sectoral supervisory policy implementation in the current macro-financial environment was attended by banking, insurance and securities supervisory authorities as well as by deposit insurers, academics and private sector representatives from around the world – more than 180 participants from 73 different jurisdictions attended the conference. Meeting participants reviewed macroeconomic, regulatory and financial developments and discussed in various panel sessions the broader policy challenges currently faced by financial authorities.

On 21 September, the FSB and the IMF published the second progress report on the implementation of phase two of the G20 Data Gaps Initiative (DGI-2). The report, which updates on the work undertaken since September 2016 to advance implementation of the 20 recommendations aimed at addressing the data gaps identified after the global financial crisis and promote the regular flow of timely and reliable statistics for policy use, has been delivered to the G20 Finance Ministers and Central Bank Governors ahead of their October meetings in Washington D.C.

The report shows substantial progress has been achieved during the first year of the DGI-2, despite challenges in the implementation of some recommendations. A new monitoring framework to help assess and track progress in implementing the 20 DGI-2 recommendations has been agreed with the G20 economies and a traffic light monitoring dashboard, included in the report, provides a concise overview of such progress. Country notes explain in more detail specific accomplishments and challenges in each jurisdiction.

To facilitate further progress, the 2018 DGI-2 work programme will continue to include thematic workshops to support participating economies' efforts on the implementation of the most challenging recommendations. It is intended that all DGI-2 recommendations are fully implemented by 2021. To this end, high-level political support is crucial, to ensure that adequate resources are allocated to DGI-2 implementation and more complex work streams are thoroughly and timely addressed.

Also on 21 September, IOSCO reported on the IOSCO Growth and Emerging Markets (GEM) Committee annual meeting and conference, in Sri Lanka, which was preceded by the meeting of the IOSCO Asia-Pacific Regional Committee (APRC). The two-day event attracted more than 300 participants from 50 jurisdictions. Participants discussed measures to address challenges in scaling up sustainable market-based financing, including the role of policy makers, regulators and industry participants in promoting green financing solutions within emerging markets. The role of International Financial Institutions in supporting sustainable capital markets was also reviewed.

Other substantive areas discussed included key issues and challenges regarding liquidity in emerging capital markets, as well as possible measures in promoting liquidity to help spur market growth and development. Participants also discussed how fintech is shaping capital markets and the balance between innovation and investor protection, particularly in areas such as crypto currencies and initial coin offerings (ICOs). The GEM Committee also conducted a cyber simulation exercise, developed in collaboration with market experts, to strengthen regulatory capabilities and preparedness in tackling cyber threats.

Discussions at the APRC focused on issues – including ICOs, the effective supervision of harmful but legal conduct, common enforcement challenges for the region, the impact of EU regulations on Asia-Pacific markets – and capacity building initiatives in the region.

Participants discussed measures to address challenges in scaling up sustainable market-based financing.

On 29 September, a *Framework Cooperation Arrangement* was signed between the EBA and several US financial regulatory agencies (the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the Securities and Exchange Commission (SEC), and the New York State Department of Financial Services). To promote resolution planning and cooperation for cross-border institutions, this arrangement lays out the basis for subsequent cooperation arrangements on bank crisis management and resolution between any of the EU supervisory or resolution authorities and any of the participating US agencies.

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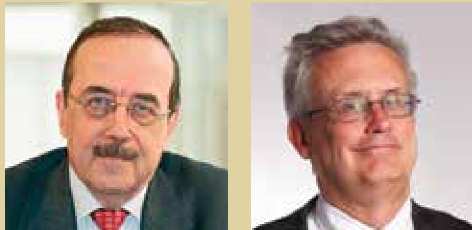

ICSA's contribution to global capital markets

By Pierre de Lauzun and Peter Eisenhardt

In response to the rapid globalization of finance, the International Council of Securities Associations (ICSA) was established in the late 1980s by securities associations from Asia, North America and Europe (including ICMA) to provide a forum to develop common regulatory positions to promote more integrated capital markets. Members also exchange views on market intelligence and industry best practices.

Over time, the International Organization of Securities Commissions (IOSCO) has played an increasingly important role in providing policy direction to independent jurisdictions in areas such as investor protection, transparency, derivatives and commodities, clearing, market conduct and cybersecurity. ICSA has engaged actively with IOSCO staff and its Standing Committees to provide an industry perspective on IOSCO policy positions and the direction of future proposals. ICSA has also worked in cooperation with the Basel Committee on Banking Supervision and the OECD.

The ICSA role as interlocutor for the global securities industry expanded dramatically in the years following the 2008 financial crisis. The G20 directions for reform, beginning in 2009, and the formation of the Financial Stability Board, set the direction and stepped up the tempo of regulatory reform, notably in OTC derivatives markets following the seizure in short-term repo and securities lending markets, the collapse in the asset-backed securities markets, the lack of adequate disclosure of derivative products and absence of centralized clearing and settlement. The G20 and FSB also focused on measures to mitigate systemic risks in the banking and shadow banking systems.

ICSA coordinated discussion and developed a consensus view among ICSA member firms on the trading and clearing reforms on OTC derivatives in Europe and the United States. ICSA was one of the first global organizations to urge greater cooperation and coordination in rule-making across jurisdictions to mitigate blockages in cross-border transactions from conflicting and duplicative regulation. Once it became evident these regulations related to trading and clearing in OTC markets were evolving in a disjointed manner and contributing to market fragmentation, ICSA endorsed remedial solutions such as regulatory recognition and jurisdictional deference, substituted compliance and passporting, as solutions to lower regulatory barriers and lower costs.

As a priority initiative, ICSA assisted in the formation of and provided the Secretariat for a global financial consultation group – the Cross-Border Regulation Forum (CBRF) – in response to the IOSCO decision to strike a Task Force on Cross Border Regulation. The CBRF published two papers, one in mid-2014 setting out a fundamental position on cross-border reform and a second in early 2015 in response to a formal IOSCO consultation paper. IOSCO recognised the value of ICSA's practical inputs which contributed to their final recommendations.

ICSA's Emerging Markets Committee has had much success on a number of fronts, such as setting out a framework for building functional credit markets, developing derivatives markets, and analysing the process of regulatory impact assessment in emerging countries.

In 2015, ICSA completed a process of incorporation to create a solid structure for the future.

To maintain high levels of engagement, ICSA has instituted a programme of biannual meetings with both IOSCO and the FSB. ICSA organizes bilateral meetings with Standing Committee Chairs at the IOSCO annual conference.

Recently, ICSA has responded to consultations on liquidity, conduct, and implementation of regulations. ICSA has provided authorities and regulators with valuable insights by surveying its global membership on topics such as culture and conduct, cybersecurity, transparency, and MiFID II implementation.

ICSA is looking forward to bringing together its members at the Interim Meeting on 15 November in London.

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European financial regulatory reforms

With the UK leaving the EU, a significant number of market infrastructures and the corresponding activity will be located outside the EU, whilst they will remain of the utmost importance for EU financial markets. Within the EU27, it is considered that this reinforces the need to build the CMU and increases the importance of third country issues for EU financial markets. In this context, on 7 July 2017, ESMA wrote to the European Commission, setting out its views on recent proposals for improvements in the way the EU deals with third countries on financial services. ESMA also highlights further areas where changes should be considered including the third country regimes for CRAs, TRs, benchmarks and possibly trading venues and data providers.

Then, on 13 July, ESMA published three Opinions, setting out sector-specific principles in the areas of investment firms, investment management and secondary markets, aimed at fostering consistency in authorisation, supervision and enforcement related to the relocation of entities, activities and functions from the UK. These Opinions, building on the general opinion issued in May, are practical tools to support supervisory convergence in the context of requests from UK financial market participants seeking to relocate to the EU27. They are addressed to NCAs and are relevant for market participants considering relocating. They provide guidance to NCAs aimed at ensuring a consistent interpretation of the requirements relating to authorisation, supervision and enforcement in order to avoid the development of regulatory and supervisory arbitrage risks. In addition, on 11 July, EIOPA issued principles on supervisory approach to the relocations from the UK.

As reported in this section of Issue 46 of the ICMA Quarterly Report, on 8 June, the European Commission announced its adoption of the Mid-Term Review of its Capital Markets Action Plan. On 11 July, the European Council announced its conclusions on this Commission Communication, which it welcomed. Among other points, the Council underlined the continued relevance of the CMU as a project of shared importance for all Member States and its continued strong commitment to the CMU. The Council looks forward to examining the legislative proposals and the delegated acts announced in the Communication and supports the inclusion of the new priority initiatives proposed by the Commission, which aim to further strengthen the CMU. The Council also looks forward to discussing the Commission's proposals for amendments to the ESAs framework, noting that supervisory convergence and the role played by the ESAs in that regard are relevant in the context of establishing an effective CMU and a sound and efficient EU financial market as a whole.

The European Commission proposed reforms to pave the way for further financial integration and a full CMU.

On 20 September, the European Commission proposed reforms to pave the way for further financial integration and a full CMU, by way of further reform of the EU's supervisory architecture. Once adopted, the proposals are intended to improve the mandates, governance and funding of the three ESAs, alongside targeted changes to the composition and organisation of the ESRB. To ensure a uniform application of EU rules and promote a true CMU, the proposals also entrust ESMA with direct supervisory power in specific financial sectors. The reforms are intended to promote further capital market integration following the UK's departure from the EU and they also introduce changes to the supervisory relations with non-EU countries, with the intention of ensuring proper management of all financial-sector risks.

Key features of the proposal are highlighted as being:

- *Stronger coordination of supervision across the EU:* the ESAs will set EU-wide supervisory priorities, check the consistency of the work programmes of individual supervisory authorities with EU priorities and review their implementation. They will also monitor authorities' practices in allowing market players to delegate and outsource business functions to non-EU countries. In addition, EIOPA will have a stronger role in promoting convergence in the validation of the internal models that some large insurance companies use to calculate requirements on solvency capital. Finally, the functioning of the ESRB will be made more efficient in order to strengthen its oversight of risks for the financial system as a whole.
- *Extended direct capital markets supervision by ESMA:* the Commission proposes to make ESMA the direct supervisor over certain sectors of capital markets across the EU: (i) capital market data – ESMA will authorise and supervise the EU's critical benchmarks and endorse non-EU benchmarks for use in the EU; (ii) capital market entry – ESMA will be in charge of approving certain EU prospectuses and all non-EU prospectuses drawn up under EU rules; (iii) capital market actors –

ESMA will authorise and supervise certain investment funds with an EU label (EVCFs, ESEFs and ELTIFs); and (iv) market abuse cases – ESMA will have a greater role in coordinating market abuse investigations, acting where certain orders, transactions or behaviours give rise to well-founded suspicion and have cross-border implications or effects for the integrity of financial markets or financial stability in the EU.

- *Improved governance and funding of the ESAs*: the ESAs will take decisions more independently from national interests, acting through newly-created Executive Boards with permanent members to deliver quicker, more streamlined and EU-oriented decisions. Interested parties will be able to ask the Commission to intervene if the majority consider that the ESAs have exceeded their competences when issuing guidelines or recommendations. The reform will also make the funding of the ESAs independent from national supervisors – while the EU budget will continue to contribute a share of the ESAs' funding, the rest will be funded by contributions from the financial sector.
- *Promoting sustainable finance and FinTech:* as the EU steps up efforts to complete the CMU, supervision has to keep pace with new market developments, notably: (i) the ESAs will promote sustainable finance, while ensuring financial stability – they will take account of ESG-related factors and risks in all the tasks they perform; and (ii) the ESAs will prioritise FinTech and will coordinate national initiatives to promote innovation and strengthen cybersecurity, while taking account of technological innovation in all the tasks they perform.

On 29 September, the EBA published its opinion on the design and calibration of a new prudential framework for investment firms, which is specifically tailored to the needs of investment firms' different business models and inherent risks. The opinion includes a series of recommendations aiming to develop a single and harmonised set of requirements that are reasonably simple, proportionate and relevant to the nature of investment firms authorised to provide MiFID services and activities. The EBA has developed this opinion in response to the European Commission's call for advice, of 13 June 2016, on the design of a new prudential framework for those MiFID investment firms for which the current prudential regime of the CRD and CRR is not appropriate.

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Financial benchmarks

On 5 July 2017, ESMA published its first Q&A on practical questions regarding the implementation of the EU Benchmarks Regulation (BMR). These Q&A included two answers regarding the transitional provisions under the BMR, clarifying which benchmarks supervised entities will be allowed to use after 1 January 2018 thanks to the transitional provisions. The purpose of this document is to be a practical convergence tool used to promote common supervisory approaches and practices in the application of the BMR; and it should also help investors and other market participants by providing clarity on the requirements.

On 29 September, ESMA then published an updated Q&A on practical questions on the BMR. The additional questions cover points on (a) the scope of the BMR: (i) application of the BMR to EU and third country central banks; and (ii) exemption on single reference price; and (b) definitions of the BMR: (i) "family of benchmarks"; and (ii) "use of a benchmark". ESMA will periodically review and, where required, update these Q&A.

Alongside this, also on 29 September, the European Commission published three adopted delegated regulations supplementing the BMR, which specify:

- technical elements of the definitions laid down in paragraph 1 of Article 3 of the BMR;
- how the criteria of Article 20(1)(c)(iii) are to be applied for assessing whether certain events would result in significant and adverse impacts on market integrity, financial stability, consumers, the real economy or the financing of households and businesses in one or more Member States; and
- how the nominal amount of financial instruments other than derivatives, the notional amount of derivatives and the net asset value of investment funds are to be assessed.

Subsequently, on 3 October, the European Commission published a further delegated regulation with regard to the establishment of the conditions to assess the impact resulting from the cessation of or change to existing benchmarks.

In addition, on 29 September, ESMA launched a consultation, for comment by 30 November, on guidelines detailing the obligations which apply to non-significant benchmarks under the BMR. The consultation proposes lighter requirements for non-significant benchmarks, their administrators and their supervised contributors in relation to four areas: (i) procedures, characteristics and positioning of oversight function; (ii) appropriateness and verifiability of input data; (iii) transparency of methodology; and (iv) governance and control requirements for supervised contributors.

As described in more detail above, on 20 September, the European Commission proposed reforms to pave the way for further financial integration and a full CMU, by way of further reform of the EU's supervisory architecture. One element within these proposals is to amend the EU BMR with a number of delegated acts to further specify some of its

provisions. If adopted as proposed, this would establish ESMA as competent authority for administrators of critical benchmarks, alongside the abolition of currently required colleges of supervisors, and of all benchmarks that are used in the EU but administered outside. The amendments would also ensure that equivalence with the BMR by third countries is monitored on an ongoing basis.

As reported in this section of Issue 46 of the ICMA Quarterly Report, on 28 April, the Bank of England revealed that the Sterling Overnight Index Average (SONIA) had been chosen as the preferred near risk-free interest rate (RFR) benchmark for use in sterling derivatives and relevant financial contracts; and that, on 29 June, an associated broad market consultation was launched. A roundtable on Sterling RFRs was held in London, on 6 July. Opening remarks were delivered by Mark Carney, Governor of the Bank of England and Chair of the FSB, followed by a speech, *The Bank and Benchmark Reform*, delivered by Chris Salmon, Executive Director, Markets, Bank of England and then by opening remarks from François Jourdain, Chair of the Sterling RFR Working Group. Subsequent panel sessions reviewed the choice of RFR for sterling markets; and the adoption of SONIA: opportunities and challenges.

Subsequently, on 27 July, Andrew Bailey, Chief Executive of the FCA, gave a speech on *The Future of LIBOR*. His key message was that hard work has been done to maintain and improve LIBOR, aimed towards the, better and more reliable, destination of interest rate benchmarks that are based on transactions, not on judgements. Yet it is considered that the journey to transaction-based benchmarks will not be completed if markets continue to rely on LIBOR in its current form and that markets cannot rely on LIBOR continuing to be available indefinitely. Work must therefore begin in earnest on planning transition to alternative reference rates that are based firmly on transactions. Panel bank support for current LIBOR until end-2021 will enable a transition that can be planned and can be executed smoothly; but the planning and the transition must now begin. (Implications for the primary bond markets are outlined in an article in the international capital market features section of this ICMA Quarterly Report).

On 21 September, the Financial Services and Markets Authority (FSMA – the Belgian financial regulatory agency), ESMA, the ECB and the European Commission announced the launch of a new working group tasked with the identification and adoption of a risk-free overnight rate which can serve as a basis for an alternative to current benchmarks used in a variety of financial instruments and contracts in the euro area. The working group, chaired by a private sector representative and with the Secretariat to be provided by the ECB, will regularly consult market participants and end-users, as well as gather feedback from other public authorities. Its terms of reference will be made public and the group will regularly report on its meetings. This is to ensure transparency on all steps in the identification and adoption of a new risk-free rate (RFR).

Ensuring broad market acceptance is vital for the effective functioning of any alternative to existing benchmark rates. Once it has made a recommendation on its preferred alternative risk-free rate, the group will also explore possible approaches for ensuring a smooth transition to this rate, if needed in the future. For such a case, careful transition planning by market participants aims to minimize disruption to markets and consumers and to safeguard the continuity of contracts to the greatest extent possible, including contracts that currently reference a term rate rather than an overnight rate. These tasks require the involvement of public authorities and a concerted effort by all market participants to facilitate a gradual reduction of the current reliance on the IBORs. The signatory public authorities reiterate that existing rates must continue to be provided in a robust and reliable manner. The signatory public authorities therefore express their appreciation for the continued commitment of those banks contributing to the EURIBOR and EONIA benchmarks and expect that they will remain supportive of these benchmarks as necessary.

The ECB also announced, on 21 September, that it will start providing an overnight unsecured index before 2020. This widens the set of options for the choice of such alternative rates for the euro area and is in line with the recommendation of the Market Participants Group of the Financial Stability Board Official Sector Steering Group's (FSB OSSG) to identify and adopt one or more risk-free rates in each main currency area. This interest rate will be based entirely on transactions in euro that are reported by banks in accordance with the ECB's money market statistical reporting (MMSR). The high-level features of this new overnight interest rate will be communicated to market participants in the course of 2018. They will then be invited to provide their feedback on the suggested approach. Additionally, the ECB will provide more information on money market activity. Based on the MMSR, aggregated rate and volume data will be released for various money market segments and tenors. The purpose of such regular publications will be to enhance market transparency and therefore improve money market functioning.

Alongside these press releases, the ECB also published an explainer, *Why are Benchmark Rates So Important?*

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Credit rating agencies

On 18 July 2017, the Joint Committee of the three ESAs launched a public consultation (for comment by 18 September) to amend the Implementing

Regulations on the mapping of credit assessments of External Credit Assessment Institutions (ECAIs) for credit risk. In these ITS the ESAs have specified an approach that establishes the correspondence, or mapping, between credit ratings and the credit quality steps defined in the EU CRR and Solvency II. Since these ITS were adopted, in 2016, ESMA has recognised five additional CRAs and withdrawn the registration of one, thus triggering the need for consequential amendment of the ITS (the mappings for the other 25 ECAIs remain unchanged). A public hearing on these draft ITS was held at the EBA, on 4 September.

Also on 18 July, the EBA published a revised decision confirming the quality of unsolicited credit assessments assigned by certain ECAIs for calculating institutions' capital requirements, again responsive to the changed population of EU CRAs (in addition, the revised decision also considers an ECAI that issued only solicited ratings when the earlier EBA decision was published, in 2016, and started issuing unsolicited ratings subsequently). Institutions may use unsolicited credit assessments of an ECAI for determining their capital requirements only if the EBA has confirmed that those unsolicited ratings do not differ in quality from solicited ratings of that same ECAI.

Furthermore, on 18 July, the EBA published its future work plan on credit assessments issued by ECAIs. Besides its ongoing work on the mapping of ECAIs' credit assessments, the EBA plans to strengthen the monitoring and quality of such mapping used for the determination of capital requirements. The EBA intends to carry out its work on ECAIs following a step by step approach; and the first phase of the workplan, which focuses on the production of mappings and the treatment of unsolicited credit assessments for newly registered or certified ECAIs, is ongoing.

The second phase, which focuses on the monitoring of existing mappings, has started and will continue over time to ensure that the underlying credit assessments continue to reflect and predict the risks of rated exposures in a consistent manner across rating agencies. Under the umbrella of the Joint Committee, the three ESAs will engage with ECAIs in due course, in particular to gather information on developments registered by ECAIs since their mappings were produced

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OTC (derivatives) regulatory developments

On 5 July 2017, the FSB, CPMI and IOSCO published three guidance documents as part of their joint (April 2015) workplan on CCP resilience, recovery and resolvability, marking the completion of the key substantive priorities set out in that workplan:

(i) *CCP resilience guidance* (CPMI and IOSCO) provides further guidance on the PFMI's *Principles and Key Considerations* regarding financial risk management for CCPs, in particular on governance, credit and liquidity stress testing, coverage, margin, and a CCP's contributions of its financial resources to losses.

(ii) *CCP recovery guidance* (CPMI and IOSCO) updates 2014 guidance on recovery for financial market infrastructures, to provide clarifications in four areas: (i) operationalisation of recovery plans; (ii) replenishment of financial resources; (iii) non-default related losses; and (iv) transparency with respect to recovery tools and how they would be applied.

(iii) *CCP resolution guidance* (FSB) finalises guidance which complements the FSB *Key Attributes of Effective Resolution Regimes* by providing guidance on implementing the Key Attributes in CCPs' resolution arrangements - this sets out powers for resolution authorities to maintain the continuity of critical CCP functions; details on the use of loss allocation tools; and steps authorities should take to establish crisis management groups for relevant CCPs and develop resolution plans.

At the same time, together with the BCBS, these three Committees also published two associated joint reports:

(i) *Interdependencies study:* this provides a first joint comprehensive data collection, covering 26 CCPs from 15 jurisdictions, that analyses the interdependencies between CCPs and their clearing members and other financial service providers. The network relationships analysed in this report are generally characterised by a core of highly connected CCPs and financial institutions and a periphery of less highly connected CCPs and financial institutions. Financial resources provided to CCPs are concentrated at a small number of CCPs and exposures to CCPs are concentrated among a small number of institutions. This study will help guide further work on CCP resolution; and by the end of 2018 an assessment will be made of the value of regular data collections from CCPs to support authorities' understanding of CCP interdependencies.

(ii) *Implementation report:* this provides an update on the work undertaken to complete the key substantive priorities set out in the joint workplan. It also reports on the establishment of crisis management groups for CCPs that are systemically important in more than one jurisdiction and sets out new actions, including further work on CCP interdependencies and on the financial resources needs of CCPs in resolution and treatment of CCP equity in resolution. Based on further analysis and experience

gained in resolution planning, the FSB will determine by end-2018 whether there is a need for additional guidance on financial resources for CCPs in resolution.

On 10 July, ESMA issued final RTS regarding the aggregation and publication of derivatives data by TRs. ESMA's RTS define the operational standards for aggregation and comparison of aggregate position data across TRs; and ensure that the market activity in derivatives traded both on and off venue is correctly identified and aggregated. The RTS are setting out several additional requirements to better specify and enhance the data quality made available publicly by TRs and also to allow the publication of certain aggregated figures that are required by MiFID II and the BMR.

In order to ensure that the end-users are able to aggregate and compare the aggregate position data published by TRs, ESMA's RTS establish general rules by defining:

- the frequency and timeliness of publication;
- the general technical aspects of aggregation for the purposes of publication; and
- the details of aggregations for the purposes of benchmarks' and commodities' thresholds

Under EMIR, derivative contracts are to be reported from both sides. This often includes several parties such as brokers and clearing members, which stand between the counterparty and the CCP. In order to ensure a good quality of data, further to the breakdowns per asset class and contract type, additional data per type of venue of execution, reporting and cleared status have been included.

The final RTS also includes further clarifications related to the publication of data by TRs, specifically on:

- calculation of market activity and outstanding volumes for on and off-venue traded derivatives;
- the avoidance of double counting across different trade repositories.

ESMA has sent its final RTS to the European Commission, which has three months to decide whether, or not, to endorse them.

On 20 July, ESMA announced that is has established an MoU, effective as of 21 June 2017, with the Securities and Exchange Board of India. This MoU establishes cooperation arrangements, including the exchange of information, regarding CCPs which are established and authorised or recognised in India, and which have applied for EU recognition under EMIR. EMIR provides for cooperation arrangements between ESMA and the relevant non-EU authorities whose legal and supervisory framework for CCPs have been deemed equivalent to EMIR by the European Commission.

ESMA's list of CCPs authorised to offer services and activities in the EU, in accordance with EMIR, was last updated on 30 August, and its list of third-country CCPs recognised to offer services and activities in the EU was last updated on 9 October. ESMA's *Public Register for the Clearing Obligation* under EMIR was last updated on 31 August; whilst its (non-exhaustive) list of CCPs established in non-EEA countries which have applied for recognition has not been updated since 18 April.

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 2 October.

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Market infrastructure

ECB: Advisory Groups on market infrastructure

The AMI-SeCo, the ECB's new advisory group on securities and collateral market infrastructure, held its second regular two-day meeting on 4-5 July 2017. A summary of the meeting as well as all the relevant documents have been published on the ECB website. Members covered again a wide range of topics, including issues related to T2S but also market infrastructure developments and initiatives more broadly. In relation to T2S, the group reviewed the latest status of the T2S operations and programme and received updates from the different sub-groups. Another key focus of the meeting was on the various ongoing harmonisation activities, including external work undertaken by the EPTF, the European Commission's post-trade expert group (see below), as well as the ambitious ECB initiative to further harmonise and streamline collateral management arrangements in Europe (see box). The ICMA ERCC is represented in the group through Nicholas Hamilton, Co-Chair of the ERCC Operations Group.

The second market infrastructure related advisory group set up by the ECB, AMI-Pay, had its latest meeting on 29 September 2017. This was the third regular meeting of this group, which focuses on questions related to the payments infrastructure in Europe. The related documents have not been published yet, but should be available shortly alongside publications from the previous two sessions. The final meetings of the year of AMI-SeCo and AMI-Pay will take place from 6-8 December in Frankfurt and will include a joint session of the two groups.

HSG Collateral Management Harmonisation Task Force (CMH-TF)

At its inaugural meeting in March 2017, the AMI-SeCo agreed to launch detailed work to achieve more harmonised collateral management processes in Europe. This takes up an initiative started in 2015 by COGESI, the AMI-SeCo's predecessor group. Besides fostering the efficient functioning of collateral management more broadly, the work is also meant to support ongoing work to develop a Eurosystem Collateral Management System (ECMS) which aims to replace the currently still fragmented collateral framework based on the Correspondent Central Banking Model (CCBM). At the meeting, AMI-SeCo members invited the Harmonisation Steering Group (HSG) to establish a list of key activities that could merit harmonisation, following a similar approach as the extensive T2S harmonisation agenda. At their subsequent meeting held on 8-9 June, HSG members reviewed a first list of 20 proposed Collateral Management Harmonisation Activities (CMHAs) and discussed the way forward with this important initiative.

Given the complexity of collateral management and the required expertise to work on the matter, it was decided to establish a dedicated HSG task force on collateral management harmonisation (CMH-TF). Industry experts, including from the ICMA ERCC, were called upon to join the CMH-TF and its five sub-streams which were established to work on the collateral management harmonisation activities, divided as follows:

- Triparty Collateral Management
- Corporate Actions, Non-EUR Collateral Management, Taxation Forms
- Bilateral Collateral Management
- Fee and Billing Processes, Reporting, Cut-Off Times
- Collateral Dynamic and Static Data.

The ICMA ERCC is actively contributing to the work, closely collaborating with ISLA. A joint ICMA/ISLA working group has been established with the three members that represent both associations on the CMH-TF. The ECB's timeline of the work is ambitious, aiming to present the first tangible conclusions at the next AMI-SeCo meeting on 7-8 December.

ECB: Other market contact groups

Members of the Bond Market Contact Group (BMCG) had their latest quarterly meeting on 16 May 2017 in Frankfurt. A summary of the meeting as well as the presentations are available on the website. The next regular BMCG meeting was held on 10 October 2017. The agenda for the meeting includes, besides the usual review of the general bond market and issuance outlook, an exchange of views on the impact of MiFID II/R on euro area bond markets, as well as a discussion on sovereign risk concentration and the state of primary dealership.

The Money Market Contact Group (MMCG) last met on 26 September 2017 in Frankfurt. No documents have been published yet. However, the documents from the previous meeting held on 13 June in Milan are now available on the website, including presentations from Bayern LB on the role of the Eurosystem's securities lending facility, by the ECB on developments in the FX swap market and by Barclays on the past, present and future of EONIA and EURIBOR. The next quarterly MMCG meeting will be held on 4 December 2017.

The ECB Operations Managers Group (ECB OMG) had its latest regular meeting on 5 October 2017. While no documents are available yet from that meeting, a summary and presentations from the previous meeting of the group held on 2 June are now available. This includes a presentation by GFMA on the impacts of MiFID II on FX markets, an ECB update on the FX Global Code as well as a presentation by Santander on the Enterprise Ethereum Alliance, a new industry initiative to develop standards and use cases around Ethereum distributed ledger technology. The next meeting of the ECB OMG is scheduled for 12 December.

ECB: Ongoing initiatives related to market infrastructure

As previously reported, the ECB is working on several significant market infrastructure related initiatives, in close coordination with the market infrastructure related advisory groups. There are broadly four separate but interconnected initiatives. Three of these have been developed as part of the Eurosystem's vision of future market infrastructure in Europe, namely: (i) a consolidation of TARGET2 and TARGET2-Securities (T2S); (ii) settlement services to support instant payments (TIPS); and (iii) a potential Eurosystem collateral management system (ECMS).

Work on all three initiatives is progressing, but is most advanced for the TIPS initiative for which a final decision was taken in June with a view to start operating the service in November 2018. The integration of TARGET2 and T2S services is

also advancing well. Detailed user requirements have been developed by a dedicated task force and subsequently published for public consultation, which closed on 30 June. A useful summary of the changes and the expected impacts on T2S was presented by the ECB at the latest AMI-SeCo meeting. Finally, the ECMS project is currently being developed by an internal task force, but, is also closely linked to the parallel work on collateral management harmonisation covered above in more detail. A helpful first overview of the expected impacts on market participants was presented to the AMI-SeCo in July.

These three concrete projects are complemented by the more strategic ECB initiative related to distributed ledger technology (DLT). The ECB continues to closely monitor developments in this space and the potential impacts on post-trade integration and harmonisation. The ECB's DLT Task Force worked over the past months on a detailed report on this topic for the AMI-SeCo which was published in September 2017.

ECB: TARGET2-Securities (T2S)

The fifth and final T2S migration wave was successfully concluded on 18 September 2017 and saw the onboarding of the Spanish and the Baltic markets. Nearly 10 years after the official launch of the T2S project in 2008, all 22 CSDs that initially committed to migrate are now connected to the single European settlement platform. T2S now settles an average of 550,000 transactions per day, making it one of the largest security settlement platforms in the world.

On the occasion of the successful roll-out of the final migration, the ECB published an article reflecting on the role of T2S and its impact on the creation of a single capital market in Europe. This includes interviews with Jesús Benito, CEO of Iberclear, and Indars Ascuks, Associate Vice-President and Head of Baltic Markets at Nasdaq, who also takes the opportunity to explain the significance of the recent merger of the three Baltic CSDs.

While this concludes the technical roll-out of T2S, work continues on the extensive T2S harmonisation agenda, covering 24 activities which are considered critical to reap the full benefits of the common settlement platform. The most recent assessment of harmonisation progress to date was published on 15 September 2017 in the form of the Mid-year update 2017.

European Commission: Post Trade consultation

On 23 August 2017, the Commission published a consultation paper on *Post-trade in a Capital Market Union: dismantling barriers and strategy for the future*. The consultation follows up on the work undertaken by the European Post-Trade Forum (EPTF), an Expert Group established by the Commission in early 2016 as part of the broader CMU project to review remaining barriers in the post-trade space. Alongside the consultation paper, the Commission thus also published the final documents prepared by the EPTF: the Final EPTF Report, which highlights remaining barriers and sets out concrete proposals to tackle them, as well as an Annex with a detailed description of the current post-trade landscape in Europe.

The Commission's consultation paper itself includes two main sections: a first part with general questions on EU and global trends, new technologies and competition in post-trade, and a second part more specifically focused on the remaining post-trade barriers identified in the EPTF report.

ICMA, represented through ERCC Chairman Godfried De Vidts, has been a member of the EPTF and has actively contributed to the final report. As an EPTF member, the ERCC is also planning to prepare a response to the consultation, and will use this opportunity to highlight some of the key priorities from our perspective, including some important issues, eg related to collateral mobility and intraday liquidity management, which are covered in the so-called watchlist section of the EPTF report highlighting potential future barriers that require close monitoring.

ESMA: Post-trading

On 24 August 2017, ESMA published final guidelines on the transfer of data or portability between Trade Repositories (TRs). The guidelines have been published in the context of EMIR, but will also be an important precedent for other TR based reporting regimes, such as SFTR.

While ESMA's work on the CSDR Level 2 measures was concluded in February 2016 with the submission of the draft technical standards on settlement discipline (currently still under review by the Commission), the work on so-called Level 3 measures continues. This includes guidelines, recommendations and Q&As. On 10 July, ESMA launched a consultation on guidelines regarding the reporting of internalised settlement. The 16 responses to the consultation received by the deadline on 14 September are available on ESMA's website. ESMA also recently published several documents in relation to the supervision and authorisation of CSDs. This includes guidelines on the cooperation between authorities published on 11 July, as well as practical guidance for the recognition of third-country CSDs by ESMA published on 28 September. A useful overview of all the implementing measures adopted under the CSDR is available on ESMA's website.

Meanwhile, the authorisation process for CSDs under the new regulatory framework is under way. CSDs have time until the end of September to submit their application to competent

authorities, who then have another six months to review the application and grant (or reject) authorisation. The related Register of CSDs authorised under the CSDR is already available on the ESMA website. The list so far includes one CSD, the Latvian CSD (as part of Nasdaq CSD SE), who already concluded the process and is the first CSD authorised under the new CSDR rules.

The global harmonization of data for OTC derivatives reporting remains among the key priorities for CPMI and IOSCO.

Global Legal Entity Identifier System (GLEIS)

The number of LEIs issued continues to grow in the face of the rapidly approaching implementation date of MiFID II/R on 3 January 2018. As previously reported, firms subject to MiFIR transaction reporting obligations will not be able to execute a trade on behalf of a client who is eligible for an LEI and does not have one. Importantly, this requirement also applies to third country entities that are otherwise not subject to MiFID rules or under any obligation to obtain an LEI.

By the end of September, 580,000 LEIs had been issued by Local Operating Units (LOUs) around the globe. Not surprisingly, the pace of issuance has picked up recently as illustrated for instance in the second quarterly GLEIS Business Report, published on 13 July. However, there are still concerns that LOUs might face a last-minute rush for LEIs ahead of MiFID II implementation causing delays in the issuance process.

On 27 September, the GLEIF announced the implementation of a new LEI application programming interface (API) to allow the industry faster and more customised access to the LEI database and facilitate automation. The full list of all LEIs issued to date continues to be freely accessible on the GLEIF website through the LEI search tool. For a more detailed overview of recent developments in relation to LEIs, regular news updates are published on the GLEIF blog, most recently in August 2017.

BIS: Committee on Payments and Market Infrastructures (CPMI)

The global harmonization of data for OTC derivatives reporting remains among the key priorities for CPMI and IOSCO. This includes work on unique identifiers, such as the Unique Transaction Identifier (UTI) and the Unique Product Identifier (UPI). On 28 September, CPMI-IOSCO published their latest report in this context, the final technical guidance on the harmonisation of the UPI. This complements similar guidance in relation to the Harmonisation of the UTI published in February 2017. Further related reports are expected to follow in the coming months covering other critical OTC derivatives data elements. CPMI-IOSCO's work is complemented by the FSB, looking at the related governance frameworks for unique identifiers. In March 2017, the FSB launched a consultation on UTI governance. This was followed more recently by a consultation paper on UPI governance, published on 3 October.

CPMI and IOSCO also continue to jointly monitor progress in the implementation of the 2012 *Principles for Financial Market Infrastructures* (PFMI). Monitoring is done at three levels in parallel. On 14 July, CPMI-IOSCO published a fourth update to their initial Level 1 assessment report, which is based on self-assessments by individual jurisdictions on how they have implemented the different PFMIs. As compared to the previous 2016 update, the report shows that some further progress has been made, with now 20 of the 28 jurisdictions found to have completed their implementation measures for all types of FMIs. In parallel, CPMI and IOSCO continue to monitor jurisdictions' progress at Levels 2 and 3. The latest report in the series of Level 2 reports analysing the completeness of individual jurisdictions' implementation measures and their consistency with the PFMI was published on 18 July, focussing on Singapore. This complements similar reports already published for Hong Kong, Japan, the US, Australia, and the EU.

On 30 August 2017, the BIS published an updated methodology for its annual statistics on cashless payments and financial market infrastructures, the so-called Red Book which covers all 24 CPMI jurisdictions. The new methodology mainly reflects recent developments in the payments space, such as online, contactless and fast payments as well as the role of non-banks and will be used for the first time as a basis for the 2018 Red Book.

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Macroprudential risk

On 4 July 2017, the EBA published an update of its *Risk Dashboard*, summarising the main risks and vulnerabilities in the EU banking sector through a set of Risk Indicators in 1Q 2017. Together with the Risk Dashboard, the EBA published the results of its Risk Assessment Questionnaire, which includes the opinions of banks and market analysts on the risk outlook between April and May this year. In 1Q 2017, EU banks' common equity tier 1 ratio remained high, albeit a modest decrease of 10 basis points (bps) to 14.1% was observed; and the average liquidity coverage ratio was 144.9% in December 2016, well above the 80% threshold defined as the 2017 liquidity coverage requirement.

Capturing financial network linkages and contagion in stress test models are important goals for banking supervisors and central banks responsible for micro- and macroprudential policy. However, granular data on financial networks is often lacking, and instead the networks must be reconstructed from partial data. *The Missing Links: A Global Study on Uncovering Financial Network Structures from Partial Data* is an ESRB working paper, published on 14 July, in which the authors conduct a horse race of network reconstruction methods using network data obtained from 25 different markets spanning 13 jurisdictions. Their contribution is two-fold: first, they collate and analyse data on a wide range of financial networks; and, second, they rank the methods in terms of their ability to reconstruct the structures of links and exposures in networks.

On 17 July, the ESRB published a report on the financial stability implications of IFRS 9 (*Financial Instruments*), which concludes that IFRS 9 represents a major improvement in comparison with IAS 39 (*Financial Instruments: Recognition and Measurement*) and is expected to bring substantial benefits from a financial stability perspective. The ESRB report also contains policy considerations to prevent or mitigate any potential negative financial stability implications of IFRS 9. The ESRB report is accompanied by the ESRB Occasional Paper No. 12 *Assessing the Cyclical Implications of IFRS 9 – a Recursive Model*.

Published on 24 July, *Macroprudential Policy Spillovers: A Quantitative Analysis* is an IMF staff working paper, which analyses cross-border macrofinancial spillovers from a variety of macroprudential policy measures, using a range of quantitative methods. Event study and panel regression analyses find that liquidity and sectoral macroprudential policy measures often affect cross-border bank credit, whereas capital measures do not. This empirical evidence is stronger for tightening than for loosening measures, is distributed across credit leakage and reallocation effects, and is generally regionally concentrated. Consistently, structural model based simulation analysis indicates that output and bank credit spillovers from sectoral macroprudential policy shocks are generally small worldwide, but are regionally concentrated and economically significant for countries connected by strong trade or financial linkages. This simulation analysis also indicates that countercyclical capital buffer adjustments have the potential to generate sizeable regional spillovers.

Published on 28 July, the sixth Annual Report of the ESRB covers the period between 1 April 2016 and 31 March 2017. In the review period, the ESRB continued its close monitoring of vulnerabilities in the EU financial system and contributed to the related policy debate. The ESRB paid particular attention to two overriding areas of risk, the continued low interest rate environment and residential real estate. The ESRB also expanded its capacity to monitor the non-banking sector, including through its publication of the first edition of an annual EU Shadow Banking Monitor. Furthermore, the ESRB was closely involved in fostering the discussion on macroprudential policy by hosting a number of conferences and workshops.

An occasional paper published by the ESRB, on 31 July, presents *A New Database for Financial Crises in European Countries*, which is intended to serve as an important step towards establishing a common ground for macroprudential oversight and policymaking in the EU. The database focuses on providing precise chronological definitions of crisis periods to support the calibration of models in macroprudential analysis. An important contribution of this work is the identification of financial crises by combining a quantitative approach based on a financial stress index with expert judgement from national and European authorities. A preliminary assessment of the performance of standard early warning indicators based on the new crises dataset confirms findings in the literature that multivariate models can improve compared to univariate signalling models

On 31 July, EIOPA published its *updated Risk Dashboard*, based on 1Q 2017 data (from the financial stability and prudential reporting of a sample of 93 insurance groups and 3,076 solo insurance undertakings). The results show that the risk exposure of the EU insurance sector remained overall stable in Q1 2017, with Solvency II ratios remaining strong and stable for groups whereas a slight deterioration has been observed particularly for solo non-life insurance undertakings. Volatility has decreased and global inflation rates are fluctuating near the 2% medium-term inflation target. Despite these positive signs, the continuing low-yield environment and the observation that market fundamentals might not properly

Market and credit risks, as a result of geopolitical, growth and debt concerns, continued to be very high.

reflect the underlying credit risk are still important concerns for the EU insurance industry.

On 11 August, the EBA published 12 indicators and underlying data from the 35 largest institutions in the EU, whose leverage ratio exposure measure exceeds €200 billion. In 2015, the number of banks with a leverage ratio exposure measure exceeding €200 billion was 36 and 3 banks have changed in the sample. This end-2016 data contributes to the internationally agreed basis on which a smaller subset of banks will be identified as G-SIIs, following the BCBS and FSB final assessments.

A stable sample of 33 institutions shows that aggregate values for over-the-counter (OTC) derivatives decreased by 8% from end-2015 and by 28% from end-2013, while for Trading and Available for Sale Securities, the total amount decreased by 7% from end-2015 and by 33% from end-2013. Total exposures for these 33 institutions, as measured for the leverage ratio, observed a decrease by 2.1% and stood at €24.6 trillion at the end of 2016.

On 17 August, the ESRB published two reports which serve as input into ongoing discussions on strengthening the prudential framework for insurers. The report on regulatory yield curves and macroprudential consequences proposes changes to the derivation of the risk-free yield curves that are used to determine the value of insurers' liabilities under Solvency II. The proposed set of changes would increase the resilience of the insurance sector. The report on recovery and resolution for the insurance sector advocates a harmonised recovery and resolution framework for insurers across the EU. Such a framework would ensure that failures in the insurance sector could be managed in an orderly way.

On 12 September, ESMA published Trends, Risks and Vulnerabilities No. 2, 2017, covering market developments from January to June 2017 and providing an outlook for the next reporting period. Overall, ESMA's risk assessment for the second half of 2017 remains unchanged from 1H 2017, with high asset price valuations seen as being the major risk for European financial markets in the coming period. Market performance during the period reflected increasing market confidence and improved expectations on the future economic outlook in EU and globally.

Market and credit risks, as a result of geopolitical, growth and debt concerns, continued to be very high, while liquidity and contagion risks remained stable but high. The outlook on operational risk remains elevated but the outlook is now negative due to heightened concerns around cyber security. Substantive risk sources include: economic growth in the EU and elsewhere that needs to prove resilient; structural problems in many EU member states continuing to be addressed; internationally, rising public and private debt levels of increasing concern; persistence of high asset price valuations; and prevailing geo-political and political uncertainties. Brexit-related uncertainties remain among the most important political sources of risk.

Also on 12 September, the BCBS published the results of its latest Basel III monitoring exercise, based on data as of 31 December 2016 – which for the first time provides not only global averages but also a regional breakdown for many key metrics. Data have been provided for a total of 200 banks, comprising 105 large internationally active banks ("Group 1 banks", defined as internationally active banks that have Tier 1 capital of more than €3 billion, which includes all 30 G-SIBs); and 95 "Group 2 banks" (ie banks that have Tier 1 capital of less than €3 billion or are not internationally active).

On a fully phased-in basis, this data shows that all banks in the sample meet both the Basel III risk-based capital minimum CET1 requirement of 4.5% and the target level CET1 requirement of 7.0% (plus any G-SIB surcharges). Additionally, of the banks in the LCR sample, 91% of the Group 1 banks (including all G-SIBs) and 96% of the Group 2 banks reported an LCR that met or exceeded 100%, while all Group 1 and Group 2 banks reported an LCR at or above the 70% minimum requirement that was in place for 2016; and, 94% of the Group 1 banks (including all G-SIBs) and 88% of the Group 2 banks in the NSFR sample reported a ratio that met or exceeded 100%, while 100% of the Group 1 banks and 96% of the Group 2 banks reported an NSFR at or above 90%.

Alongside this, on 12 September, the EBA published its twelfth report of the CRDIV-CRR/Basel III monitoring exercise on the European banking system, based on data as of 31 December 2016. Overall, the results show a further improvement of European banks' capital positions, with a total average CET1 ratio of 13.4% (12.8% as of 30 June 2016) – this exercise does not reflect any BCBS standards agreed since the beginning of 2016 or any other measures currently being considered by the BCBS. The analysis of leverage ratio (LR) shows that there has been

a continuous increase in the last periods, with estimated LR at 5.0% (4.7% as of June 2016).

On the liquidity side, the average LCR was 139.5% (133.7% as of June 2016), while 99.2% of the banks in the sample show a LCR above the full implementation minimum requirement applicable from January 2018 (100%); and, on a Basel basis, the analysis shows an overall average NSFR ratio of 112.0% (107.8% as of June 2016), with around 87.5% of participating banks already meeting the minimum NSFR requirement of 100%.

Legislators need to be mindful that authorities require a broad range of tools to be able to tackle risks beyond the banking sector.

Published by the BIS on 17 September, *What are the Effects of Macroprudential Policies on Macroeconomic Performance?* is a special feature included in the latest BIS Quarterly Review. While macroprudential policies are designed to make financial crises less likely or less severe, at the same time, they might also curb output growth by affecting credit supply and investment. Using data for a panel of 64 advanced and emerging market economies, this special feature investigates empirically the effects of macroprudential policies on long-run economic performance. The authors find that countries that more frequently use macroprudential tools, other things being equal, experience stronger and less volatile GDP growth; and that these effects are influenced by each economy's openness and financial development. Finally, they find that non-systematic macroprudential interventions tend to be detrimental to growth.

On 21 September, the Joint Committee of the ESAs published its Autumn 2017 *Report on Risks and Vulnerabilities in the EU's Financial System*. The Report highlights the risks to the stability of the European financial sector in an uncertain political and economic environment, not least in light of the UK's withdrawal from the EU. It also highlights persistent valuation risk with an uncertain outlook for yields and argues that financial institutions continue to face profitability challenges in spite of recent improvements. Rapid developments in the area of FinTech are raising new opportunities, but also challenges for financial institutions and final users. The Report also presents regulatory and supervisory initiatives to monitor and mitigate the risks identified.

The second ESRB annual conference was held in Frankfurt, on 21-22 September. In his opening keynote address Mario Draghi, in his capacity of Chair of the ESRB, outlined that much has been achieved since the global financial crisis. In particular, banks in Europe are more resilient and the banking union has advanced. Moreover, authorities have the mandates and tools to tackle risks in the banking sector and are using them. These improvements have created a financial system that poses fewer risks to the real economy, yet, at the same time, work remains to be done. Authorities need to watch out for blind spots, where risks can build up unnoticed, and use the tools at their disposal. And legislators need to be mindful that authorities require a broad range of tools to be able to tackle risks beyond the banking sector.

In his keynote speech Commission Vice-President Valdis Dombrovskis briefly touched on the macro-economic situation and NPLs in particular, before discussing the Commission's newly published proposal for a review of the ESFS – starting with micro-prudential aspects, and ending with the macro-prudential aspects. This package of proposals seeks to make improvements where necessary without upsetting the balance of what proved to be functioning. At the same time, it is ambitious in seeking to enhance the ability of the ESFS, and the ESAs in particular, to play a key role going forward. On the second day, Tobias Adrian, IMF Financial Counsellor gave a speech about macroprudential policy and financial vulnerabilities. Overall, he highlighted that the monitoring of financial conditions and vulnerabilities provides useful information about downside risks to GDP in the short and medium run, thus usefully guiding the stance of policy.

Besides the speeches, sessions during the conference, involving a mix of senior academics, officials and industry participants, examined legal perspectives on macroprudential regulation; the challenges and future of banking in the EU; addressing non-performing loans in the EU banking sector; identifying and assessing risks in the shadow banking system; and macroprudential policy beyond banking. At the end of the conference, the winners of the ESRB Research Prize, awarded annually to recognise outstanding research conducted by young scholars on a topic related to the ESRB's mission, presented their

research, *Compressing OTC Markets*, and were formally awarded their prize.

As announced on 28 September, the General Board of the ESRB held its 27th regular meeting on 21 September. The General Board continues to highlight the repricing of risk premia in global financial markets as the main risk to EU financial stability. Despite solid prospects of recovery in the real economy, tail risks remain elevated amid high geopolitical and policy uncertainties, both in Europe and in the global economy as a whole. The General Board also considered insights from research papers analysing EU derivatives markets data from trade repositories.

Also on 28 September, the ESRB released the 21st issue of its risk dashboard. Overall, this reports that market based measures of systemic stress in the EU have remained at low levels. Considering macro risk, economic recovery in the EU has continued in the second quarter of 2017; unemployment remains high in some EU countries, but continues its downward trend; and although most countries have deleveraged in the past years following the global financial crisis, debt levels remain elevated across countries and sectors in the EU.

Regarding credit risk, bank lending both to households and to NFCs in the EU continued to increase, while the cost of borrowing for both households and NFCs remains low. Looking at financial sectors, banks' profitability in the EU improved in the second quarter of 2017, but remains, on average, low; and the median capitalisation of EU banks increased in the second quarter of 2017. And, the size of the non-banking part of the EU financial sector increased over the past year relative to the total assets of credit institutions, but was stable in the first quarter of 2017.

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FinTech and government bonds in Kenya

At the time of publication of the previous article, the Kenyan Treasury initiated the issuance of a larger tranche of the "M-Akiba", a government bond that is exclusively purchased and traded via mobile phones. The initial aim was to raise €8.5 million (KES 1 billion), which subject to demand, was to be increased to up to €32.5 million (KES 3.85 billion).

However, due to a lack of demand by retail investors, the three-week issuance window was extended from 21 July to 8 September 2017. Investors were initially given the choice between two payment providers, one of which failed to gain traction among banks and investors. Furthermore, it appeared to be difficult to capture investors' attention amid the presidential elections held in August.

As a result, the bond offer was undersubscribed and, by its new closing date, only €1.95 million (KES 240 million) or 25% of the initial volume had been purchased by over 300,000 retail investors. The bond subsequently became tradable on the secondary market, exclusively via mobile phones, on the Nairobi Stock Exchange from 12 September 2017.

Nonetheless, this is an interesting case study which demonstrates how existing technology can be leveraged to provide innovative solutions. ICMA will continue to follow the evolution of mobile phone bond trading and other innovative FinTech initiatives.

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ICMA Capital Market Research

Use of Leverage in Investment Funds in Europe
Published: 19 July 2017
Authors: ICMA 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

Closed for Business: A Post-Mortem of the European Repo Market Break-Down over the 2016 Year-End
Published: 14 February 2017
Author: Andy Hill, ICMA

The Counterparty Gap: A study for the ICMA European Repo and Collateral Council on the Trade Registration Models used by European Central Counterparties for Repo Transactions
Published: 27 September 2016
Author: Prepared for ICMA by John Burke, independent consultant

Remaking the Corporate Bond Market: ICMA's 2nd Study into the State and Evolution of the European Investment Grade Corporate Bond Secondary Market
Published: 6 July 2016
Author: Andy Hill, ICMA

Evolutionary Change: The Future of Electronic Trading in European Cash Bonds
Published: 20 April 2016
Author: Elizabeth Callaghan, ICMA

Perspectives from the Eye of the Storm: The Current State and Future Evolution of the European Repo Market
Published: 18 November 2015
Author: Andy Hill, ICMA

Impact Study for CSDR Mandatory Buy-ins
Published: 24 February 2015
Author: Andy Hill, ICMA

The Current State and Future Evolution of the European Investment Grade Corporate Bond Secondary Market: Perspectives from the Market
Published: 25 November 2014
Author: Andy Hill, ICMA

Continually Working to Develop Efficient and Effective Collateral Markets
ERC Occasional Paper
Published: 4 September 2014
Author: David Hiscock, ICMA

Covered Bond Pool Transparency: the Next Stage for Investors
Published: 21 August 2014
Author: Prepared for ICMA by Richard Kemmish Consulting Ltd

Collateral is the New Cash: The Systemic Risks of Inhibiting Collateral Fluidity
Published: 3 April 2014
Author: Andy Hill, ICMA

Avoiding Counterproductive Regulation in Capital Markets: A Reality Check
Published: 29 October 2013
Author: Timothy Baker, Senior Adviser to ICMA

Collateral Damage: the Impact of the Financial Transaction Tax on the European Repo Market and its Consequences for the Financial Markets and the Real Economy
Published: 8 April 2013
Author: Richard Comotto, ICMA Centre

Economic Importance of the Corporate Bond Markets
Published: 8 April 2013
Author: Timothy Baker, Senior Adviser to ICMA

Events & Education

Supporting interbank markets in Africa

ICMA and Frontclear have signed an MoU to strengthen their partnership on the supply of technical expertise for the development of interbank markets in frontier economies.

Frontclear is a financial markets development company focused on catalysing stable and inclusive interbank markets in emerging and frontier markets. ICMA has worked with Frontclear in the past on its technical assistance programme which is directed towards developing market knowledge. ICMA has supplied expertise and training on repo including workshops on implementing and understanding the Global Master Repurchase Agreement.

Under the new agreement ICMA will support Frontclear's objectives in the interbank market by providing further technical workshops on the GMRA in Kenya, Uganda, Ghana and Zambia during 2018

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IWN
ICMA Women's Network
Networking. Progression. Support.

ICMA Women's Network launch in Luxembourg

The IWN recently partnered with the European Investment Bank's (EIB) "ConnectedWomen" network at an event hosted by the EIB in Luxembourg. Entitled "Starting Out". This event, attended by close to 90 guests, comprised a panel expertly moderated by Shirin Wheeler from the Media Office of the EIB, and featuring Julie Becker (Member of the Management Board of the Luxembourg Stock Exchange), Luc Caytan (Senior Representative of ICMA), Kalin Anev Janse (Secretary General of the European Stability Mechanism) and Eila Kreivi (Director, Capital Markets at the EIB).

The panel started with a look back at their "defining moments". Ranging from setting up a dealing room team from scratch in a foreign country, moving abroad with little knowledge of the local language or culture, frequently changing functions within an organisation to starting a family, these turning points in their careers taught the panellists that, while one cannot plan too much into the future, taking chances can only make one stronger and prove that anything is possible.

Not that the panellists did not encounter obstacles on their way. The panel agreed that, while some of these obstacles may be strewn in one's path, such as work practices that are not compatible with domestic arrangements, others can be self-imposed, such as a lack of self-belief, a negative mindset, poor efficiency and time management skills, and a lack of assertiveness. But stay true to yourself – when it comes to leadership qualities, the panel converged on the point that leadership is about being authentic, being yourself, and showing character and strength.

It was largely agreed that women should not need to be apologetic about imposing their agenda and challenging the perceptions which are instilled at an early age – the gender stereotyping whereby it is accepted that boys will be raised to expect a career, while girls will be happy to wait in the wings. Instead, society should be encouraged to review its thinking and offer ambition and choice to all – by way of changing accepted work practices, as well as mindset at a societal as well as a management level. Whether this can be achieved by imposing quotas or targets is a moot point – ultimately, the right candidate should be employed notwithstanding their gender - but either way, the message needs to come from the top, ensuring that women are in line for the same opportunities as men, and quotas can be a tool to achieve that aim.

Asked what advice they would impart to those embarking on their careers, a number of themes emerged: the importance of building competences and experiences as early as possible in life, which can form the foundations of a strong and stable career strategy later on; why it is vital to have the confidence to believe in yourself, and to make the most of every opportunity (poetically articulated as "taking a front row seat in life"); why we should always nurture relationships made through networking; why we should not be afraid of asking questions and, importantly, to smile through it all – which automatically emits positivity!

The panel was followed by a very animated and extended structured networking session, all set amid an exhibition of striking modern art installations. Feedback from this event was extremely positive, with many guests registering interest in future IWN and Connected Women events, which ICMA hopes to be able to facilitate in 2018.

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Diary 2017

DATE	
15 November *Register*	**ICMA Women's Network & UniCredit's UniONE: Challenging Perceptions: Unconscious bias – how it affects networking & career progression, London, 15 November** Unconscious bias training has become a standard feature of workplace diversity programmes, but outside the formal office environment, is our tendency to make snap judgements based on stereotypes affecting the way we network? This joint event from the ICMA Women's Network and the UniONE Diversity Committee of UniCredit will take a practical look at how unconscious bias may be subtly influencing our ability to make and maintain the contacts that we need to help us progress in our careers.
2 December *Register*	**ICMA Future Leaders Networking Reception, Paris, 2 December** ICMA Future Leaders (IFL) with Natixis will be hosting an event in Paris to encourage networking among young professionals in the banking and finance sector. The event will feature a number of senior industry practitioners who will address the topic: *What's the Deal? The Changing Relationship between Employers and Employees.*

ICMA Workshops

19 October 26 October 27 October *Register*	**ICMA MiFID II/R Implementation Workshops** ICMA has been running a series of workshops for its members focusing on the transparency, best execution and the research obligations of MiFID II/R, as well as the newly emerging market structure trends, such as innovative protocols and platforms. MiFID II/R Implementation Workshop schedule: • 19 October: Madrid • 26 October: Frankfurt • 27 October: Milan
1 November *Register*	**Bond syndication practices for compliance professionals and middle office professionals, London, 1 November** 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.
8-10 November *Register*	**Repo and securities lending under the GMRA and GMSLA, London, 8-10 November** 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.
20-21 November *Register*	**GMRA Masterclass – a clause-by-clause analysis & Annex I negotiation, London, 20-21 November** This two-day advanced-level workshop systematically reviews the Global Master Repurchase Agreement (GMRA) 2011 clause by clause, giving a thorough grounding in all of its key provisions and the most commonly-used Annexes.

Diary 2017

DATE	ICMA Conferences
31 October *Register*	**Opportunities and Challenges of Internationalisation of the Chinese Capital Market, Shanghai, 31 October** Hosted by ICMA, Shanghai Lujiazui Financial City Development Authority and Zhong Lun Law Firm, this half day conference will look at the latest developments in Chinese capital markets, covering: green bonds, capital market financing for the belt and road, panda bonds and Bond Connect.
2 November *Register*	**Developments in Green and Social Bond Markets – the Asian perspective, Tokyo, 2 November** The conference will build on the sharp growth in Asian green bond activity, the recent launch of guidelines by the Japanese Ministry of Environment, pioneering social bond issuance, and increased regional investment in such products.
8 November *Register*	**ICMA Asset Management and Investors Council Conference, London, 8 November** The AMIC meeting, open to all on the buy side, is held twice a year and offers an opportunity to find out what the international investment community is thinking about on a range of market issues.
8 November *Register*	**The 11th ICMA Primary Market Forum, London, 8 November** The ICMA Primary Market Forum, is the definitive event where issuers, syndicate banks, law firms and investors come together to discuss market trends and practices, regulatory developments and the overall outlook for the primary debt capital markets.
14 November *Register*	**ICMA European Repo and Collateral Council General Meeting, Brussels, 14 November** The Autumn 2017 General Meeting will be used as an opportunity to deepen the exchange of ideas between the market, the public sector and academia at this critical time in the post-crisis programme of regulatory reform.

Save the Date!

For the 50th ICMA AGM and Conference: Madrid, 30 May to 1 June 2018

For more information, please contact: ICMAevents@icmagroup.org or visit www.icmagroup.org/events

Courses 2017

Five reasons why an ICMA foundation course is for you!

1. No previous knowledge needed: Our foundation courses are designed for people starting out in their careers in finance, each one will take you right through from the basics to a professional level of understanding, giving you skills and knowledge to use daily in your job and preparing you for further study with our Advanced courses.

2. Expert teachers: Our tutors have real-world experience in financial markets as well as sound academic knowledge. Over the course of our 3-day classroom programme you can ask questions on any concepts, analytics or processes that you don't understand. (It will also give you the chance to spend 3 days in a classroom with international professionals from different firms working in the same area of finance, what better opportunity is there to grow your worldwide network!)

3. Industry-wide recognition: Our foundation courses are recognised by the CFA as part of their Continuing Professional Education Programme – when you study with us you are keeping your knowledge and skills incontestably up to date.

4. From a well-respected organisation: All our foundation courses are respected by employers in the international industry. When you pass the exam, you will have a qualification from a highly regarded organisation which will be a real asset as you go on to develop your career.

5. Available online: We also run the Financial Markets Foundation Course and the Securities Operations Foundation Qualification online, so if you prefer, you can study at your own pace and gain the same qualification.

Foundation Qualifications

Financial Markets Foundation Qualification (FMFQ) Online
Next start date: **1 November 2017 (registration deadline 30 October)**

Securities Operations Foundation Qualification (SOFQ) Online
Next start date: **1 November 2017 (registration deadline 30 October)**

Introduction to Primary Markets Qualification (IPMQ)
London: **29 November – 1 December 2017**

Introduction to Fixed Income Qualification (IFIQ)
London: **11-13 October 2017**

Securities Operations Foundation Qualification (SOFQ)
Brussels: **15-17 November 2017**

Financial Markets Foundation Qualification (FMFQ)
London: **6-8 November 2017**

Advanced Qualifications

ICMA Fixed Income Certificate (FIC) Online
Next start date: **1 November 2017 (registration deadline 30 October)**

ICMA Operations Certificate Programme (OCP)
Brussels: **20-24 November 2017**

ICMA Fixed Income Certificate (FIC)
Amsterdam: **23-27 October 2017**

ICMA Primary Market Certificate (PMC)
London: **27 November – 1 December 2017**

Training Programmes

Collateral Management
London: **25-26 October 2017**

Trading the Yield Curve with Interest Rate Derivatives
London: **18-19 October 2017**

Corporate Actions – An Introduction
London: **2-3 November 2017**

Credit Default Swaps – Pricing, Application & Features
London: **28-29 November 2017**

Credit Default Swaps – Operations
London: **30 November 2017**

Securitisation – An Introduction
London: **22-23 November 2017**

Securities Lending & Borrowing – Operational Challenges
London: **11-12 December 2017**

The ICMA Guide to Best Practice in the European Repo Market
London: **27 November 2017**

Fixed Income Portfolio Management
London: **9-10 November 2017**

Inflation-linked Bonds and Structures
London: **13-14 November 2017**

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

ABCP Asset-Backed Commercial Paper
ABS Asset-Backed Securities
ADB Asian Development Bank
AFME Association for Financial Markets in Europe
AIFMD Alternative Investment Fund Managers Directive
AMF Autorité des marchés financiers
AMIC ICMA Asset Management and Investors Council
ASEAN Association of Southeast Asian Nations
AuM Assets under management
BBA British Bankers' Association
BCBS Basel Committee on Banking Supervision
BIS Bank for International Settlements
BMCG ECB Bond Market Contact Group
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
COGESI Contact Group on Euro Securities Infrastructures
COP21 Paris Climate Conference
COREPER Committee of Permanent Representatives (in the EU)
CPMI Committee on Payments and Market Infrastructures
CPSS Committee on Payments and Settlement Systems
CRA Credit Rating Agency
CRD Capital Requirements Directive
CRR Capital Requirements Regulation
CSD Central Securities Depository
CSDR Central Securities Depositories Regulation
DLT Distributed ledger technology
DMO Debt Management Office
D-SIBs Domestic systemically important banks
DVP Delivery-versus-payment
EACH European Association of CCP Clearing Houses
EBA European Banking Authority
EBRD European Bank for Reconstruction and Redevelopment
ECB European Central Bank
ECJ European Court of Justice
ECOFIN Economic and Financial Affairs Council (of the EU)
ECON Economic and Monetary Affairs Committee of the European Parliament
ECP Euro Commercial Paper
ECPC ICMA Euro Commercial Paper Committee
EDGAR US Electronic Data Gathering, Analysis and Retrieval
EEA European Economic Area
EFAMA European Fund and Asset Management Association
EFC Economic and Financial Committee (of the EU)
EFSF European Financial Stability Facility
EFSI European Fund for Strategic Investment
EFTA European Free Trade Area
EGMI European Group on Market Infrastructures
EIB European Investment Bank
EIOPA European Insurance and Occupational Pensions Authority
ELTIFs European Long-Term Investment Funds
EMDE Emerging market and developing economies
EMIR European Market Infrastructure Regulation
EMTN Euro Medium-Term Note
EMU Economic and Monetary Union
EP European Parliament
ERCC ICMA European Repo and Collateral Council
ESA European Supervisory Authority
ESG Environmental, social and governance
ESCB European System of Central Banks
ESFS European System of Financial Supervision
ESMA European Securities and Markets Authority
ESM European Stability Mechanism
ESRB European Systemic Risk Board
ETF Exchange-traded fund
ETP Electronic trading platform
ESG Environmental, social and governance
EU27 European Union minus the UK
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
FSB Financial Stability Board
FSC Financial Services Committee (of the EU)
FSOC Financial Stability Oversight Council (of the US)
FTT Financial Transaction Tax
G20 Group of Twenty
GBP Green Bond Principles
GDP Gross Domestic Product
GMRA Global Master Repurchase Agreement
G-SIBs Global systemically important banks
G-SIFIs Global systemically important financial institutions
G-SIIs Global systemically important insurers
HFT High frequency trading
HMRC HM Revenue and Customs
HMT HM Treasury
HQLA High Quality Liquid Assets
HY High yield
IAIS International Association of Insurance Supervisors
IASB International Accounting Standards Board
ICMA International Capital Market Association
ICSA International Council of Securities Associations
ICSDs International Central Securities Depositaries
IFRS International Financial Reporting Standards
IG Investment grade
IIF Institute of International Finance
IMMFA International Money Market Funds Association
IMF International Monetary Fund
IMFC International Monetary and Financial Committee
IOSCO International Organization of Securities Commissions
IRS Interest rate swap
ISDA International Swaps and Derivatives Association
ISLA International Securities Lending Association
ITS Implementing Technical Standards
KfW Kreditanstalt f r Wiederaufbau
KID Key information document
KPI Key performance indicator
LCR Liquidity Coverage Ratio (or Requirement)
L&DC ICMA Legal & Documentation Committee
LEI Legal Entity Identifier
LIBOR London Interbank Offered Rate
LTRO Longer-Term Refinancing Operation
MAD Market Abuse Directive
MAR Market Abuse Regulation
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
PD Prospectus Directive
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
RFR Risk-free interest rate
RM Regulated Market
RMB Chinese renminbi
ROC Regulatory Oversight Committee of the Global Legal Entity Identifier System
RPC ICMA Regulatory Policy Committee
RSF Required Stable Funding
RSP Retail structured products
RTS Regulatory Technical Standards
RWA Risk-weighted assets
SEC US Securities and Exchange Commission
SFT Securities financing transaction
SGP Stability and Growth Pact
SI Systematic Internaliser
SLL Securities Law Legislation
SMEs Small and medium-sized enterprises
SMPC ICMA Secondary Market Practices Committee
SMSG Securities and Markets Stakeholder Group (of ESMA)
SPV Special purpose vehicle
SRB Single Resolution Board
SRM Single Resolution Mechanism
SRO Self-regulatory organisation
SSAs Sovereigns, supranationals and agencies
SSM Single Supervisory Mechanism
SSR EU Short Selling Regulation
STORs Suspicious transactions and order reports
STS Simple, transparent and standardised
T+2 Trade date plus two business days
T2S TARGET2-Securities
TD EU Transparency Directive
TFEU Treaty on the Functioning of the European Union
TLAC Total Loss-Absorbing Capacity
TMA Trade matching and affirmation
TRs Trade repositories
UKLA UK Listing Authority
VNAV Variable net asset value

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