ICMA

International Capital Market Association

QUARTERLY REPORT

ASSESSMENT OF MARKET PRACTICE AND REGULATORY POLICY

INSIDE:

THE BREXIT NEGOTIATIONS AND THE INTERNATIONAL CAPITAL MARKETS

FINTECH AND MARKET ELECTRONIFICATION

SUSTAINABLE FINANCE

12 April 2018

Second Quarter. Issue 49. Editor: Paul Richards

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 60 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.

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A landmark year for ICMA

By Juan Blasco

As we mark the 10th anniversary of the start of the one of the most profound financial crises in history, it is a good time to reflect on the evolution of capital markets and to take this opportunity to shape our industry for the years to come.

This year also coincides with the implementation of the highest regulatory agenda in many years. MiFID II/R is the culmination of a series of measures taken by regulators to strengthen the financial sector and make markets more transparent and resilient.

With the benefit of hindsight, we now understand that financial innovation and regulation should work hand in hand to provide the best solutions for clients and to ensure well-functioning capital markets. Arguably, one of the core reasons for the crisis was a too loose financial innovation context whereas, on the other hand, a too rigid regulatory environment could discourage capital and intellectual investment in our industry. It is paramount as well that incentives and values are always aligned.

We also need to understand the current business environment with the rapid development in financial technology and the many opportunities that the digital transformation offers.

As a landmark year, 2018 also marks ICMA´s 50th anniversary, celebrated with a number of events such as the magnificent commemorative dinner held last February in London and the next AGM and Conference we will hold in Madrid at the end of May. This will be a great opportunity for capital market professionals to "deep dive" on the topics that will determine the development of our industry during the years that follow.

We have an impressive agenda for the Conference this year with a solid set of speakers from the public and private sectors that will cover the main topics of focus for ICMA. Primary and secondary, repo and collateral as well as green and social markets will be the main themes of our annual gathering. These and undoubtedly other topics for discussion, such as the normalisation of monetary policy and its effect on markets and the future growth of private markets, will also be part of many of our conversations.

And, of course, all with a common denominator: change. The years to come will bring an unprecedented amount of change on the back of political and regulatory implementations (Capital Markets Union and Brexit being the most imminent), technological developments (such as automation or blockchain) and social and environmental considerations. How we embrace these changes and use them as an opportunity will determine the future of capital markets in their role of fostering economic growth.

In Madrid we will also have an opportunity to learn more about progress on the different initiatives in which ICMA is heavily involved. The Market Practice and Regulatory Policy group has been busy focusing on the recent regulatory changes and will continue to work with ICMA members to navigate a way through regulatory developments. The new focus on FinTech and market electronification covering all the aspects of the lifecycle of securities will help us understand the opportunities that the digital transformation will offer. Responsible financing is a very encouraging positive development that continues to grow at a phenomenal pace. ICMA's role in helping to establish the Green Bond Principles and the Social Bond Principles has been key for the growth of this market and a reference for all financing products, such the recently published LMA Green Loan Principles.

The ICMA Women's Network has been actively engaged in fostering diversity through a series of initiatives and events across many countries.

Looking ahead, we should also think about what new skills future capital market professionals will need. The Future Leaders and the Mentoring Platform are not only great initiatives for our young leaders to network and develop, they are also fora for future generations actively to engage in addressing how our industry continues to be an attractive proposition for the best talent.

We have an opportunity to embrace change, learn from the mistakes of the past and work together with ICMA in shaping an ever-efficient capital market, inclusive, socially responsible and with the highest standards of integrity.

I look forward to seeing you in Madrid.

Juan Blasco *is Managing Director and Global Head of Syndicate, Banco Bilbao Vizcaya Argentaria, SA, and Member of the ICMA Board*

Message from the Chief Executive

By Martin Scheck

In this edition of the Quarterly Report we cover a number of major issues which consumed market participants' time and resources during 2017 and will continue to do so in 2018. Looking ahead we also comment on two of the major initiatives currently facing capital markets participants – sustainability and the IBOR transition.

As we all know, implementation of MiFID II/R on 3 January this year followed a tremendous effort by market practitioners and many of the regulatory bodies to be ready and compliant on time. On the positive side the market continued to function, and there was no significant dislocation – business was transacted throughout. But nevertheless, there are many issues which still need to be ironed out and it remains to be seen whether, in fixed income, the legislation will achieve its objectives and what its longer-term impact will be. We are continuing our regional workshops post-implementation to assess the issues being encountered now by market participants and will also be analysing data during the year as we assess the longer-term implications. Our initial findings are in the article below – not surprisingly data quality and availability feature strongly. However, the bigger structural impact will take time to emerge and we will be reviewing the evidence to see whether our concerns over the availability of new issuances of debt securities for retail investors and of SME fixed income research are validated.

ICMA has been acting as the Secretariat of the Green Bond Principles for the last four years and released the new Social Bond Principles in 2017. Since then the sustainability movement has gathered tremendous momentum and the number of market participants (and associations) involved proliferated. We have been active globally through our interactions with the G20, the authorities in China, ASEAN and other parts of the world. In Europe we were delighted to be part of the European Commission's High Level Expert Group (HLEG) on sustainable finance and contributed to its well-received report published on 31 January 2018. In early March this was followed by the European Commission's Action Plan on sustainable finance drawing upon the recommendations of the HLEG. This is an important step forward, but it will also be important to achieve the right balance between future prescriptive legislation and market-led standards and guidelines.

The previous edition's Quarterly Assessment focused on the transition from LIBOR, and here our work has intensified. ICMA was asked by the Bank of England and UK Financial Conduct Authority to chair the Bond Market Sub-Group of the Risk-Free Rate Working Group. The Sub-Group has already been constituted, agreed its terms of reference and met, and work is well under way. We have also been invited to join the Euro Risk-Free Rates Working Group, which has had its first meeting, and been asked to join the Swiss National Working Group on risk-free rates. So ICMA is well positioned to represent its members and contribute to the transition of these critical benchmarks to risk-free rates. We are also cooperating with several other trade associations in a global survey on benchmarks carried out by EY.

Finally, as many of you know, 2018 is the 50th anniversary of ICMA's founding as the Association of International Bond Dealers (AIBD). We were delighted that many of you were able to join us for a celebration dinner in February in the beautiful setting of London's Guildhall. We are in the process of finalising the arrangements for the 50th AGM and Conference in Madrid from 30 May to 1 June. Speakers and panellists are confirmed, venues, including the world-renowned Prado museum, booked and registrations are open. I hope to see you there.

Martin Scheck
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The Brexit negotiations and the international capital markets

By Paul Richards

Summary

The purpose of this paper is to assess the current state of the Brexit negotiations between the UK and the EU27 from the perspective of the international capital markets, focusing on: the transition period after Brexit; the framework for a future trade agreement; and the implications for international capital market firms operating in the UK and in the EU27.

Introduction

1 Agreement in principle was reached in December 2017 on the first phase of negotiations for the withdrawal of the UK from the EU on 29 March 2019. The agreement in principle covered:

- an agreed method for calculating the divorce bill to be paid by the UK to the EU27;
- an agreement on the rights of EU27 citizens in the UK and UK citizens in the EU27; and
- an agreement on "full alignment" as a fall-back, if no alternative is agreed, to prevent a hard border between Northern Ireland (in the UK) and the Irish Republic.[1]

2 The European Council judged in December that the agreement in principle represented "sufficient progress" to move on to the second phase of the negotiations, covering:

- *a transition period after Brexit:* the UK and the EU27 agreed at the European Council on 23 March 2018 on the terms of a transition period starting on 29 March 2019 and lasting until the end of 2020, when the EU's next multi-annual budget is due to begin;[2] and
- *the framework for a future trade agreement between the UK and the EU27:* only a framework agreement is possible before the UK leaves the EU, as the EU is not legally able to conclude an agreement with the UK as an external partner while the UK is still an EU Member State.[3]

3 In practice, the framework for a future trade agreement needs to be settled by the autumn of 2018 in order to give sufficient time for EU27 Member States, the European Parliament and Parliament in the UK to decide whether to approve the withdrawal agreement or not by the deadline of 29 March 2019. The British Government has promised

1. The European Commission published a draft Article 50 Withdrawal Agreement on 19 March 2018 translating into legal terms the progress achieved during the first stage of the negotiations, and on the transition, and proposing text for outstanding withdrawal issues which are still subject to negotiation between the UK and the EU27.

2. Michel Barnier, Chief EU Negotiator: Brussels, 9 January 2018. The British Government refers to the "transition period" as an "implementation period".

3. David Davis, Secretary of State for Exiting the EU: *Implementation Period: A Bridge to the Future Partnership Between the UK and EU:* Teesport, 26 January 2018.

Parliament a "meaningful vote" on the outcome of the negotiations. There appear to be four possible outcomes:

- The first possible outcome is for all the authorities involved to approve the withdrawal agreement, covering both the first and the second phase of the negotiations, and leading to a transition period after Brexit during which detailed negotiations can take place on a future trade agreement. This is the outcome preferred by the British Government and the EU27.
- The second possible outcome is that the withdrawal agreement is not approved by all the authorities involved. If so, there is a risk that the UK may leave the EU without an agreement. A disorderly withdrawal – over a "cliff edge" – is an outcome which both sides want to avoid.[4]
- A third possible outcome is that, before 29 March 2019, Article 50 could be extended (eg until the end of the transition period). This would require not only the support of the British Government, but also the unanimous support of the EU27. Extending Article 50 would avoid a situation in which the UK, which has participated as a "rule maker" while a member of the EU, would become a "rule taker": ie new EU rules would apply in the UK without the UK having any say in making them. However, extending Article 50 would also mean that the UK would not leave the EU until after the date at which it is publicly committed to leave. It is not clear whether this would be politically acceptable to Parliament in the UK.
- The fourth possible outcome would arise only if the British Government were to change its intention before Brexit and decide to remain in the EU. That could not happen, first of all, unless Article 50 could be revoked. The answer to this question has not been clarified by the European Court of Justice, though in practice President Tusk and President Juncker have both said that the UK could remain in the EU, if it wished to do so.[5] And second, a change of intention would probably require, not only a vote in Parliament on the outcome of the negotiations, but also a general election or a second referendum in the UK on whether to accept the outcome of the negotiations to leave or alternatively to remain. The British Government's view is that the UK is leaving the EU and "there is no question of a second referendum".[6]

The transition period after Brexit

4 Many international capital market firms have made it clear that, if they do not know at least a year in advance of Brexit whether there will be a transition period after Brexit, they will have no choice but to plan on the basis that the UK will leave the EU without an agreement. UK withdrawal without an agreement would create risks in both the UK and the EU27 of a "cliff edge", which they want to avoid. The transition period agreed at the European Council on 23 March helps to address these concerns, but there are still questions relating both to the terms and timing of the transition and also to outstanding legal issues:

(i) Transition terms and timing

5 The first question is whether international capital market firms can rely on the transition agreement for planning purposes. It is conditional on the UK/EU27 withdrawal agreement as a whole: "nothing is agreed until everything is agreed". The UK and the EU27 still need to negotiate the framework for a future trade agreement, and to resolve outstanding issues such as finding a workable solution to avoiding a hard border between Northern Ireland and the Irish Republic. While the agreement on a transition period at the European Council on 23 March is an important step in the right direction for international capital market firms, they may still regard it as prudent to continue to undertake contingency planning in case the transition period does not happen.[7] To help reassure the market, the Bank of England has stated that it "considers it reasonable for firms currently carrying on regulated activities in the UK by means of passporting rights, or the EU framework for central counterparties, to plan that they will be able to continue undertaking these activities during the implementation [ie transition] period in much the same way as now".[8]

6 The second question relates to the terms of the transition agreement. There are three related elements:

- One element is that the proposed transition agreement is

4. Michel Barnier: "On 8 December we reached an agreement with the UK that represents a significant step towards an orderly withdrawal.": Brussels, 9 January 2018. Without a deal, the UK would fall back on trading under the WTO. The WTO does not cover in any detail trade in financial services.

5. President Tusk, President of the European Council: "Our hearts are still open to you."; President Juncker: "If the UK wished to stay in the EU, they should be allowed to do so.": 16 January 2018.

6. British Prime Minister, speech at the Security Conference in Munich, 17 February 2018.

7. See also the statements by the Bank of England, PRA and FCA on 28 March 2018.

8. Bank of England: *Update on the Regulatory Approach to Preparations for EU Withdrawal:* 28 March 2018.

largely on a "standstill" basis: "unless otherwise provided in this Agreement, Union law shall be applicable to and in the UK during the transition period".[9] This should in general mean that international capital market firms need to implement only one set of changes at the end of the transition period, not two (ie one at the beginning as well as one at the end). However, the detailed implications need to be considered. For example, it is understood that the deadline previously set by the ECB for licence applications remains unchanged at the end of June this year.

- A second element is that the UK has agreed to the *status quo:* ie continuing free movement of people between the UK and the EU27; the jurisdiction of the European Court of Justice; and continuing net budgetary contributions from the UK to the EU27. However, the UK is permitted during the transition period to negotiate new trade agreements with countries outside the EU, and sign them, though it cannot implement them until after the end of the transition period.[10]
- A third element is that the UK will no longer be able to participate in EU decision-making after Brexit: ie instead of being a "rule maker", it will become a "rule taker". This has raised political concern in Parliament in the UK that, during the transition period, the UK will effectively become a "vassal state" unless steps are agreed in advance to forestall this. The draft withdrawal agreement provides for limited consultation with the UK by the EU on decisions affecting the UK, but without UK voting rights.[11]

7 The third question is whether a transition period of under two years will be long enough to complete the negotiation of a detailed trade agreement before the transition period comes to an end, and if not whether the transition period will be extended:

- The trade agreement between the EU and Canada (CETA) took seven years to negotiate and ratify. Given the scope and scale of the relationship between the UK and the EU27, a trade agreement between the UK and the EU27 is likely to be much more complex, though (unlike CETA) there will be full regulatory alignment at the start.
- A UK/EU27 agreement would be likely to need to be approved by 38 national and regional Parliaments, which would inevitably take time.
- The transition period was originally envisaged as a period in which international capital market firms were given time to implement plans for the future trade agreement between the EU27 and the UK. But if the future trade agreement cannot be negotiated in any detail until after Brexit, as the EU27 propose, the prospective outcome will not be clear for some time. That will reduce the amount of time during the transition period in which detailed implementation planning can take place, unless the transition period can be extended.

(ii) Legal issues

8 Apart from the terms of the transition, there are also several legal issues arising from Brexit where action may need to be taken by the UK and the EU27, acting together, to maintain financial stability, including three issues in particular:

- First, action may need to be taken to ensure that a wide range of financial contracts across borders between the UK and EU27 counterparts can continue to be serviced, in particular insurance and derivatives contracts, when passporting between the UK and the EU27 ceases.
- Second, action may need to be taken to ensure that EU27 and UK CCPs are not in breach of regulation by providing clearing services in the other's jurisdiction, both in order to maintain existing positions and to take on new positions.
- Third, action may need to be taken by the UK and the EU27 to ensure that holding and sharing each other's data is not in breach of national law.[12]

9 Finally, the EU Withdrawal Bill is intended to take EU law into UK law on Brexit. During the transition period after Brexit, UK law is expected to continue to follow EU law; and the UK needs to continue to participate in the EU's international agreements.[13]

The framework for a future trade agreement

10 The negotiations between the UK and the EU27 on the framework for a future trade agreement are currently

9. *Draft Agreement on the Withdrawal of the UK from the EU*, 19 March 2018: Article 122, Scope of the transition. See also David Davis, Secretary of State for Exiting the EU: "Businesses now have the certainty they asked for about life immediately after Brexit, knowing that they can trade on the same terms as they do today until the end of December 2020.": *Sunday Telegraph,* 25 March 2018.

10. David Davis, Secretary of State for Exiting the EU: "[In this period,] we can start negotiating, signing and ratifying our own trade deals."

11. *Draft Agreement on the Withdrawal of the UK from the EU*, 19 March 2018: Article 123, Institutional arrangements.

12. See Andrew Bailey, CEO, FCA: *The Future of the City,* 5 February 2018.

13. "During the transition period, the UK shall be bound by the obligation stemming from the international agreements concluded by the Union ...": Draft Agreement on the withdrawal of the UK from the EU", 19 March 2018: Article 124 on specific arrangements relating to the Union's external action. See also David Davis, Secretary of State for Exiting the EU: "The scores of international agreements we are signed up to as members of the EU should continue to apply during the implementation period." *Sunday Telegraph,* 25 March 2018.

constrained by "red lines" on both sides:

- UK "red lines" consist of: control over EU immigration; freedom to negotiate new trade agreements with the rest of the world; no jurisdiction in the UK for the European Court of Justice; and no further budgetary contributions to the EU (other than for some specific purposes) after the end of the transition period. The British Government is opposed to UK membership of the European Economic Area after Brexit; and it accepts that its "red lines" involve leaving both the EU Single Market and the Customs Union, though the Opposition is in favour of remaining in a Customs Union.[14]
- EU27 "red lines" consist of: the indivisible nature of the four EU freedoms (ie free movement of goods, services, capital and people), with no "cherry picking"; continuing budgetary contributions for market access; and the jurisdiction of the European Court of Justice.
- Both sides "want good access to each other's markets; we want competition between us to be fair and open; and we want reliable, transparent means of verifying we are meeting our commitments and resolving disputes."[15]

11 Taking account of the "red lines" on both sides, what progress can be made towards the framework for a future trade agreement? The Prime Minister set out the British Government's negotiating position in a speech at the Mansion House in London on 2 March. On financial services, the UK is seeking to be "part of a deep and comprehensive partnership" with the EU:

- "We are not looking for passporting because we understand this is intrinsic to the Single Market of which we would no longer be a member. It would also require us to be subject to a single rule book, over which we would have no say."
- "As in other areas of the future economic partnership, our goal should be to establish the ability to access each other's markets, based on the UK and EU maintaining the same regulatory outcomes over time, with a mechanism for determining proportionate consequences where they are not maintained."
- "But given the highly regulated nature of financial services, and our shared desire to manage financial stability risks, we would need a collaborative, objective framework that is reciprocal, mutually agreed, and permanent and therefore reliable for businesses."[16]

12 By contrast, the European Council guidelines of 23 March on the framework for a future free trade agreement with the UK are similar to the agreement between the EU and Canada. The European Council proposes that:

- "Being outside the Customs Union and the Single Market will inevitably lead to frictions in trade. ... A non-member of the Union, that does not live up to the same obligations as a member, cannot have the same rights and enjoy the same benefits as a member."
- "The four freedoms are indivisible and there can be no "cherry picking" through participation in the Single Market based on a sector-by-sector approach, which would undermine the integrity and proper functioning of the Single Market. ... A [free trade agreement] cannot offer the same benefits as membership and cannot amount to participation in the Single Market or parts thereof."
- "The agreement would address trade in services, with the aim of allowing market access to provide services under host state rules, including as regards right of establishment for providers, to an extent consistent with the fact that the UK will become a third country and the Union and the UK will no longer share a common regulatory, supervisory, enforcement and judiciary framework."[17]

13 The EU27's Chief Negotiator has argued that there is not a single example of a trade agreement that is open to financial services.[18] However, the EU agreements (eg with Canada, Singapore, South Korea, Switzerland and Turkey) are all with countries which have never been members of the EU, in contrast to the UK which, as a result of being a member of the EU, will start with complete regulatory alignment with the EU, including in financial services.[19] The Governor of the Bank of England has rejected the argument that, just because an agreement on financial services has not been done in the past, it cannot be done in the future;[20] and the Chancellor of the Exchequer has stated: "I am clear not only that it is possible to include financial services within a trade deal but that it is very much in our mutual interest to do so."[21] It is also relevant

14. Jeremy Corbyn, Leader of the Opposition: 26 February 2018.

15. British Prime Minister, Mansion House speech, 2 March 2018.

16. British Prime Minister, Mansion House speech, 2 March 2018.

17. European Council Guidelines: 23 March 2018.

18. Michel Barnier, Brussels, 9 January 2018.

19. Sam Woods, CEO of the PRA: "A detailed free trade agreement covering financial services could be agreed within a three-year period from now. We are fortunate in starting this discussion in the unique position in terms of having completely aligned rules and strongly aligned supervision.": 16 January 2018.

20. Mark Carney, Governor of the Bank of England: 20 December 2017.

21. Philip Hammond, Chancellor of the Exchequer: Speech at HSBC, 7 March 2018.

to note that, in the Transatlantic Trade and Investment Partnership negotiations with the US a few years ago, and in its initial proposals for CETA with Canada, the EU proposed a trade agreement which included provision for financial services.[22]

Implications for the international capital markets

14 Given the differences between the UK and EU27 negotiating positions, there is a risk that very little progress will be made in the negotiations leading up to the framework agreement before Brexit, leaving the difficult issues to be resolved during the transition period after Brexit. What would be the implications for the international capital markets?

15 A standstill transition would prolong the existing situation, but international capital market firms would be no clearer about the ultimate outcome of the negotiations: whether a future trade deal including financial services could be achieved (as the UK proposes), or whether there is a Canada-style trade deal, under which financial services would not meaningfully be covered at all (as the EU27 propose).

(i) Mutual recognition

16 The British Government considers that the best way to preserve open markets between the UK and the EU27 after Brexit would be through mutual recognition of each other's regulatory standards, given that the UK is proposing to leave the Single Market on Brexit and that, on Brexit, the UK and EU27 regulatory regimes will be the same:

- Agreement on mutual recognition would involve setting common objectives with broad equivalence of regulation in terms of outcomes, supervisory cooperation and effective information sharing.[23] An approach of this kind would also recognise the difference between the principles-based common law system in the UK and the rules-based system in the EU27. If regulatory alignment between the UK and the EU27 were to continue after Brexit and regulatory divergence were to be avoided, the result would be to maximise UK access to the EU Single Market and vice versa, and to minimise the risk of market fragmentation that would otherwise arise, with costs for both sides.[24]
- The potential criticism of this approach is that the EU27 have so far stated that they will not accept it;[25] and that, from the UK's perspective, continuing regulatory alignment after Brexit would mean that the UK would effectively be signing up to EU rules in future without any say in making them. While there would be freedom for UK regulation to diverge in future by not maintaining equivalent outcomes, there may be consequences in doing so.[26] There is also a related concern that the EU27 without UK influence in the future will be different from the EU including the UK in the past, when the UK had a significant influence over the development of the EU Single Market.
- However, cross-border rules on financial services all need to be consistent with the global approach to regulation taken by the Financial Stability Board, which both the UK and the EU27 support. The UK authorities are committed to "maintain standards of resilience at least as high as those we have today".[27] Wholesale financial markets are global and "cannot in practice diverge much in terms of regulatory outcomes; and regulatory arbitrage is not an allowable ground for competition."[28]

(ii) Alternatives to mutual recognition

17 The EU27 have so far rejected an approach based on mutual recognition of regulatory standards between the UK and the EU27. An alternative would be for the UK – as a third country – to use EU provisions for regulatory equivalence. This is currently a patchwork: it applies to some parts of the EU regulatory framework, but not others; where it does apply, it is not always complete; it requires a judgement by the European Commission as well as a

22. Philip Hammond, Chancellor of the Exchequer: Speech at HSBC, 7 March 2018.

23. Andrew Bailey, CEO, FCA: "What underpins freedom to trade is not a trade agreement of the long-established sort – it's not about the WTO, very important though the WTO is in other spheres of activity. It's not about tariffs or import quotas or licensing agreements. No. It's about mutual recognition of regulatory standards which appropriately protect the public interest: *The Future of the City,* 5 February 2018.

24. See also Philip Hammond, Chancellor of the Exchequer: "The principle of mutual recognition and reciprocal regulatory equivalence, provided it is objectively assessed, with proper governance structures, dispute resolution mechanisms, and sensible notice periods to market participants clearly could provide an effective basis for such a partnership.": Speech at HSBC, 7 March 2018.

25. President Tusk, President of the European Council: "There is no possibility to have some form of exclusive single market for some parts of our economies.": 7 March 2018.

26. Philip Hammond, Chancellor of the Exchequer: "Where rules do evolve differently we will need an objective process to determine whether they provide sufficiently equivalent regulatory outcomes. … In certain circumstances, we may choose not to maintain equivalent outcomes, but we know there may be consequences.": Speech at HSBC, 7 March 2018.

27. Sam Woods, CEO, PRA: FT, 5 February 2018.

28. Andrew Bailey, CEO, FCA: *The Future of the City,* 5 February 2018.

technical assessment, and it takes time to assess; and the determination of equivalence can be withdrawn at short notice, though this has not happened so far. The assessment of regulatory equivalence is based on measuring outcomes, but outcomes are not straightforward to measure. It is not yet clear whether, during the UK/EU27 negotiations, there will be scope to improve the arrangements for regulatory equivalence for third countries.

18 Regulatory equivalence is useful for international capital market firms, in so far as it goes. But if it is not possible to rely solely on regulatory equivalence, the other option is for firms to ensure that they are authorised to provide financial services in both the EU27 and in the UK.[29] Most large firms either have authorised operations in the EU27 already or are planning to seek authorisation to do so, as long lead times are involved. The Single Supervisory Mechanism of the ECB has stated that any bank wishing to relocate from the UK to the euro area should submit its licence application by the end of the second quarter of 2018.[30]

19 The ECB has set out the basis on which banks can relocate to the euro area:

- "After the UK has left the EU, EU branches of UK credit institutions may lose their passporting rights and will consequently no longer be allowed to operate in the EU. In order to continue any regulated activities, these institutions will need to ensure that they have an appropriate authorisation."
- "Banks in the euro area should be capable of managing all material risks potentially affecting them independently and at the local level and should have control over the balance sheet and all exposures."
- "With specific reference to the "back-to-back booking model", the ECB and national supervisors would expect that part of the risk generated by all material product lines should be managed and controlled locally."
- "The operational independence of the supervised bank should not be compromised as a result of the outsourcing of funds or services. Outsourcing arrangements will be reviewed and assessed by ECB and national supervisors on a case-by-basis."[31]

20 In addition, in the case of delegation decisions made by firms to outsource or transfer risk outside the EU27, whether to the UK or to other third countries, the European Commission is proposing to give the European Supervisory Authorities new powers to review delegation to third countries. The delegation framework under UCITS and the AIFMD enables investment funds to delegate functions such as custody and portfolio management while being subject to strict oversight and accountability by those funds' national regulators in compliance with EU rules. The EU framework requires firms to meet various conditions before they can delegate activities to ensure that they are not just "letter box" entities.[32]

21 The UK authorities have also set out their approach to supervising international capital market firms with operations in the UK:

- The UK FCA has stated: "During [the implementation (ie transition) period] EU law would remain applicable in the UK, in accordance with the withdrawal agreement. Firms and funds would continue to benefit from passporting between the UK and EEA during the implementation period. Obligations derived from EU law would continue to apply and firms must continue with implementation plans for EU legislation that is still to come into effect before the end of December 2020.[33]
- The UK PRA has stated: "Firms may plan on the assumption that PRA authorisation will only be needed by the end of the implementation period. Firms should consider how best to make use of the additional time provided by the implementation period in their planning.[34]
- The Bank of England has also stated: "The Government has committed to bring forward legislation, if necessary, to create temporary permission regimes to allow relevant firms to continue their activities in the UK for a limited period after withdrawal. In the unlikely event that the Withdrawal Agreement is not ratified, this provides confidence that a back-stop will be available."[35]

29. See Dr. Andreas Dombret, Member of the Executive Board of the Deutsche Bundesbank: "Looking at banks, proper preparation includes establishing at least basic entities in the other economic area – that is, the EU27 or the UK – in order to continue doing business there.": *The Future Relationship Between Germany and the UK in Finance After Brexit,* 8 February 2018.

30. Sabine Lautenschläger, Vice-President of the Single Supervisory Mechanism of the ECB: 7 February 2018.

31. ECB: *Relocating to the Euro Area:* FAQs, January 2018.

32. Steven Maijoor, Chair of ESMA: "We are not looking to question, undermine or put in doubt the delegation model. What our opinions are seeking to address is the risk of letterbox entities": Brussels, 20 March 2018.

33. FCA *Statement on EU Withdrawal Following the March European Council*, 28 March 2018.

34. PRA: *Firms' Preparations for the UK's Withdrawal from the EU: Update Following March European Council,* 28 March 2018.

35. Bank of England: *Update on the Regulatory Approach to Preparations for EU Withdrawal,* 28 March 2018.

(iii) Supervisory coordination

22 Coordination between UK and EU27 supervisors will be important to ensure that market disruption from Brexit is avoided, if at all possible. The Bank of England's approach to preparations for EU withdrawal is based on "the presumption that there will continue to be a high degree of supervisory cooperation between the UK and the EU."[36]

23 As a condition for authorisation to operate in the EU27, it is not yet clear to what extent EU27 supervisors will insist on the relocation of capital market activities and the market infrastructure – through the transfer of bank capital, infrastructure and staff (eg for risk management) – 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, where activities 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.[37] Indeed, avoiding financial instability would be one of the main reasons why coordination between supervisors would be necessary in the first place.

Conclusion

24 Agreement between the UK and the EU27 on a transition period after Brexit gives international capital market firms more time to prepare for the outcome of the UK/EU27 negotiations on a future trade agreement, provided that the transition period goes ahead as planned. But the agreement on a transition period does not resolve any of the difficult issues that the negotiations on a future trade agreement need to address. So ICMA members – both in the UK and the EU27 – still face considerable uncertainty in the meantime. ICMA will continue to keep members informed to the extent that it is possible to do so.

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36. The Bank of England: *Update on the Regulatory Approach to Preparations for EU Withdrawal:* 28 March 2018. See also: Philip Hammond, Chancellor of the Exchequer: Speech at HSBC, 7 March 2018.

37. Dr. Andreas Dombret, Member of the Executive Board of the Deutsche Bundesbank: "I am confident that this cooperative style [ie the proposals by the PRA and the SSM] can be an important contribution towards a smooth transition." *The Future Relationship Between Germany and the UK in Finance After Brexit*, 8 February 2018.

The European corporate single name credit default swap market

By Andy Hill and Gabriel Callsen

In February 2018, ICMA published a *Study into the State and Evolution of the European Corporate Single Name Credit Default Swap Market*. Resilient, well-functioning international debt capital markets are essential in supporting economic growth, jobs, and productivity: something that is at the core of ICMA's work. In recent years ICMA has been particularly focused on the efficiency and liquidity of European corporate bond secondary markets, the robustness of which is important not only for investors and fund managers, but also for the health of the primary market and so corporate issuers. As has been identified in this work,[1] the ability of banks and other institutions to provide liquidity in the corporate bond secondary markets is contingent not only on the availability and cost of capital to support market making, but also on their ability to access ancillary funding[2] and hedging markets.

Why this study?

A well-functioning corporate single name credit default swap (SN-CDS) market is largely recognised as an important component for developing corporate bond markets, as highlighted by recent reports by ICMA,[3] IOSCO,[4] and the European Commission Expert Group on European Corporate Bond Markets.[5] Meanwhile, there is mounting anecdotal and empirical evidence that liquidity is deteriorating in the corporate bond markets,[6] and while a number of possible causes have been identified, including regulatory impacts on market makers' capital and extraordinary monetary policy, it would seem that a parallel decline in SN-CDS market liquidity is also a contributing factor.

Scope and methodology

The study focuses primarily on the market for single name CDS referencing European entities, both corporate and financial. It applies a "triangular" research approach, utilising both quantitative analysis and qualitative interviews with market stakeholders. The data is sourced primarily from DTCC's Trade Information Warehouse (TIW), Bloomberg, as well as from ICE Clear Europe.[7] For the qualitative input, the researchers conducted semi-

1. See, for instance: ICMA, 2014, *The Current State and Future Evolution of the European Investment Grade Corporate Bond Secondary Market: Perspectives from the Market*

2. This was explored in detail in the study: ICMA, 2017, *The European Credit Repo Market: The Cornerstone of Corporate Bond Market Liquidity*

3. ICMA, 2016, *Remaking the Corporate Bond Market*

4. IOSCO, 2017, *Examination of Liquidity of the Secondary Corporate Bond Markets*

5. European Commission, 2017, *Improving European Corporate Bond Markets*

6. For example, see: Risk Control, 2017, *Drivers of Corporate Bond Market Liquidity in the European Union*

7. ICMA would also like to acknowledge the invaluable contribution of ISDA in undertaking this study, in particular for compiling the data and providing quantitative market analysis that is used extensively throughout the report.

structured interviews with a range of users and liquidity providers, including market makers, asset managers (both real money and leveraged), as well as loan book traders.

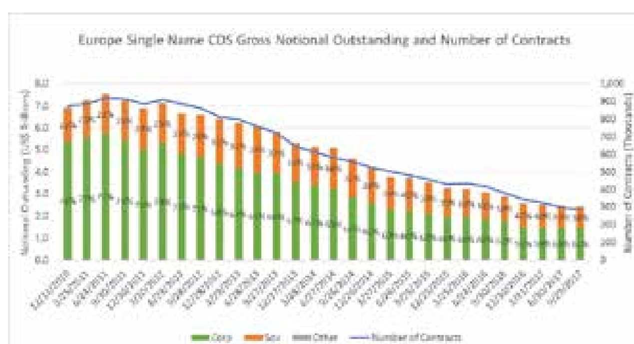
Users of the SN-CDS market

A highly efficient means of managing credit risk, corporate single name credit default swaps (SN-CDS) are used by a range of market participants, including corporate bond market makers, investors, hedge funds, loan book traders, and those managing banks' counterparty credit exposures. In addition to being an effective hedging instrument, SN-CDS can be used as an alternative means of assuming credit risk, as well as creating trading opportunities with respect to other financial instruments, and so playing a vital role in price discovery in the corporate and sovereign bond markets.

Market liquidity

A very clear message from the data and interviews is that liquidity in the corporate SN-CDS market has deteriorated significantly in the period since 2007-2008, which can largely be attributed to a retrenchment of market makers, including some high-profile actors. Interviewees suggest that there are now only four or five fully committed market makers for corporate SN-CDS in Europe, and perhaps only two-to-three active within each sector; and while these dealers continue to provide pricing and liquidity, it is too few to support a deep and liquid market.

Gross notional outstanding Europe SN-CDS



Source: ISDA analysis based on DTCC TIW data

The outstanding gross notional amount of European SN-CDS declined more than 50% from the fourth quarter of 2010 to the third quarter of 2017.[8] At the end of the fourth quarter 2010, outstanding notional totaled $6.9 trillion compared with $2.4 trillion at the end of the third quarter of 2017. The number of outstanding contracts declined from about 874,000 to 283,000 over the same period.

Dealer attrition

The attrition of market makers is in turn attributed largely to the increased capital costs of running CDS books post Basel III, as well as benign market conditions which have reduced the demand for protection, as low credit spread volatility makes it more difficult to generate profits. A number of interviewees suggest that a more volatile market environment would draw some of the recent defectors back to making markets.

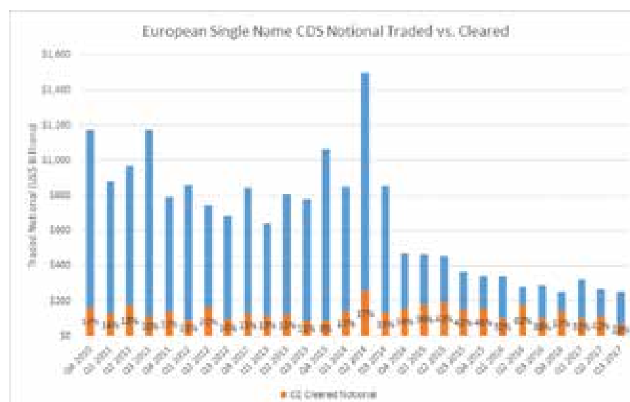
CSPP

Many interviewees cited the ECB's Corporate Sector Purchase Programme as a key dampener of volatility, while also creating asymmetric risks towards further spread tightening. Low spread volatility, as well as historically low default rates, also reduce the value placed on buying protection, which limits end-user activity.

Clearing

The discussions on central clearing for SN-CDS point to some inherent differences of opinion, or perhaps differing approaches, to clearing between sell-side and buy-side firms. While most CDS index trading in Europe is now centrally cleared, with a continuing trend away from bilateral trading, the SN-CDS market remains relatively fragmented. A greater adoption of central clearing is broadly seen as supporting improved liquidity.

ICE Clear Europe cleared SN-CDS vs notional traded



Source: ISDA analysis based on ICE Clear Europe-CDS data and DTCC TIW data

Electronic trading

Despite a trend toward greater platform-based trading of CDS indices, SN-CDS remains primarily an OTC market.

8. Gross notional represents the sum of the nominal values for CDS contracts Gross notional represents the sum of the nominal values for CDS contracts bought (or equivalently sold) for all DTCC Warehouse contracts in aggregate.

A more concerted effort by capital market participants and stakeholders to understand, embrace, and promote the corporate SN-CDS product and market would only be to the benefit of the European corporate bond market.

The improved standardisation of SN-CDS contracts, in theory, should make the product more amenable to venue trading, and both sell-side and buy-side firms are generally supportive of moving more SN-CDS trading onto platforms, both from a trade processing efficiency perspective, as well as a transparency and price discovery aspect. However, for a number of technical reasons, traction remains slow.

MiFID II/R

The advent of MiFID II/R, for the most part, is seen as a potential positive. The general view is that improved post-trade transparency should help to create more market confidence with respect to trade transparency and a sense of true liquidity. At the same time, it is also noted that greater transparency could expose the positions of market makers and act as a deterrent to provide liquidity.

ISDA definitions and trigger events

Interviewees express general satisfaction with the introduction of the 2014 ISDA Definitions for CDS, which revised the previously relied upon 2003 Definitions. In particular, respondents feel that it has helped support CDS market liquidity while also providing more certainty around default events, in particular for financials. Greater flexibility in the deliverability process is also broadly seen as a marked improvement in the overall efficient functioning of the market.

In the lead-up to and during the undertaking of this study there had been some high-profile, and largely contentious, press coverage of specific CDS trigger events. A striking message from the interviews is that, for the most part, participants seem unconcerned by the outcomes of these particular events or the final price determination, and that the contracts largely operated as they should. However, it is also widely acknowledged that it is impossible to design contracts for every possible eventuality, and that on occasion there will be unexpected or contentious outcomes. But in general, so long as market participants are prepared to commit to the necessary due diligence, or entrust experienced and knowledgeable traders and risk managers, the SN-CDS market functions relatively efficiently.

Conclusion

It is perhaps the negative perception of CDS by some commentators, and even policy makers and regulators, that creates one of the biggest challenges to revitalising a healthy European SN-CDS market, and the benefits this brings in terms of risk mitigation and in supporting vibrant corporate bond markets. CDS are inherently complex instruments, and trading and utilising them efficiently requires a degree of expertise and experience, which is at risk of being lost in today's post-reform markets. A more concerted effort by capital market participants and stakeholders to understand, embrace, and promote the corporate SN-CDS product and market would only be to the benefit of the European corporate bond market, which in turn would have positive implications for issuers, investors, and so the European economy.

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ICMA's engagement on FinTech and market electronification

By Gabriel Callsen

Introduction

FinTech[1] and market electronification[2] have been focus areas of ICMA for a number of years. Together with member firms, ICMA has undertaken substantive work across primary, secondary, repo and collateral markets. This article highlights how FinTech and market electronification have been addressed through ICMA's different constituencies and provides an overview of current initiatives.

Primary markets electronification

Whilst the uptake of technology solutions in primary markets remains limited in comparison to secondary or repo and collateral markets, it is arguably an area which offers significant potential for further electronification. In primary markets, discussions on FinTech developments, whether "conventional" or new technologies such as distributed ledger technology (DLT), have periodically been on the agenda of the Primary Market Practices Committee (PMPC), Corporate Issuer Forum (CIF), Financial Institution Issuer Forum (FIIF), and Euro Commercial Paper (ECP) Committee.

How technological developments may potentially impact market practice is a key question for ICMA. For instance, in the ECP Committee the potential evolution of the ECP market process in light of technological solutions has been addressed. Building on distributed ledger technology (DLT), which has been developed in collaboration with ING, ABN and KBC, Commerzbank completed a proof of concept for issuing ECP together with KfW Banking Group and MEAG last year. A demonstration was subsequently arranged with the ECP Committee, illustrating how DLT could conceptually be utilised to create a more streamlined process for the issuance and redemption of ECP.

Discussions around technology and opportunities to enhance the efficiency of existing ECP market practices continue. Further use cases of technology are being considered.

Secondary markets electronification

In secondary markets, ICMA continues to address electronification and automation, and their role in the evolution of market structure[3] in secondary fixed income markets. Under the umbrella of the Secondary Market Practices Committee (SMPC), the Electronic Trading Working Group (ETWG) and Platform Working Group (PWG) have focused on these topics for several years.

In the run-up to the implementation of MiFID II, members of the ETWG and regulatory experts from respective member firms came together as MiFID II Working Group to discuss the implementation of MiFID II and notably the implications for market structure, innovative trading protocols, execution and regulatory reporting requirements. To face many of the challenges of MiFID II and its impact on trading practices, joint meetings with the PWG have been held on a number of occasions.

As a result of this fruitful engagement, the ETWG and PWG are going to be merged to form the Electronic Trading Council (ETC), combining buy-side and sell-side trading representatives, along with representatives from the trading venues and technology providers, as a technical sub-group of the SMPC. As fixed income electronic trading evolves, the primary purpose for the ETC is to provide a centralised platform for dialogue to identify best practice or standards and address technical issues. The first meeting is scheduled for the second half of April 2018. The ETC is expected to inform the broader work of the SMPC and is intended to ensure that FinTech is mainstreamed into ICMA's secondary market focus and workstreams.

1. A term broadly used to describe innovation in financial services enabled by technology.

2. The rising use of technology across the securities lifecycle.

3. Here we use the term 'market structure' in the macro sense of how markets are organised and operate.

Furthermore, in light of the evolving market structure resulting from MiFID II, ICMA is in the process of reviewing and updating the mapping directory of electronic trading platforms (ETPs) and information networks. The revised version of the directory is expected to be published in Q2 2018. The ICMA ETP mapping directory remains a unique resource for the European fixed income markets.

Electronification in repo and collateral markets

The use of technology solutions for repo and collateral management operations is widespread, which is reflected in ICMA's engagement through dedicated working groups under the umbrella of the European Repo and Collateral Council (ERCC).

The ERCC Ops FinTech Working Group (WG) focuses precisely on technology solutions for repo and collateral management operations. Having launched a mapping exercise in late 2016, the Ops FinTech WG carried out the mapping throughout 2017 and published the ICMA Ops FinTech mapping directory for repo and cash bond operations in November 2017. The directory is available on ICMA's website and provides a (non-exhaustive) overview of over 100 applications across 10 categories including collateral management, intraday liquidity monitoring and reconciliation.

Based on the FinTech mapping directory, a survey is being conducted amongst members of the Working Group and the ERCC Operations Group to help determine common priorities, shared concerns or suggestions and, if required, engage with vendor firms to address operational inefficiencies in the market.

It is furthermore anticipated that the reporting obligation of repos and other types of securities financing transactions (SFTs) under the upcoming SFT Regulation will further drive electronification. ICMA's SFTR Task Force has engaged and will continue to engage with relevant stakeholders to prepare for the implementation of the reporting regime from 2019, address technology-related challenges, and allow for interoperability between technology solutions.

Electronification from a cross-cutting perspective

A consolidated view of ICMA's engagement and resources related to technology in fixed income markets can be found on ICMA's dedicated webpage, including relevant committees, working groups, and the above-mentioned ETP and FinTech mapping directories. ICMA papers and further key contributions on DLT and other FinTech developments are also available on this page.

Furthermore, the ICMA Future Leaders (IFL) Committee, which brings together individuals of ICMA member firms in the early stages of their career, has set up a dedicated IFL FinTech Working Group to complement ICMA's overall engagement in areas that have not been explored sufficiently.

Conclusion

FinTech and market electronification are themes which cut across all of ICMA's member firms and committees. Even though the level of adoption of technology varies, it is anticipated that technology will play an ever-increasing role and impact capital markets and member firms' business models.

A considerable amount of thorough work has been done and ICMA continues to work closely with members. ICMA seeks to mainstream relevant FinTech developments through all of its initiatives, activities and fora. This means identifying technology trends and anticipating the impact of technological innovation more broadly on capital markets, whilst monitoring relevant regulatory and legislative initiatives.

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The ICMA ETP mapping directory remains a unique resource for the European fixed income markets.

European Commission Action Plan on sustainable finance *By Nicholas Pfaff*

After a year of activity, the European Commission's High Level Expert Group (HLEG) on sustainable finance published its final report on 31 January. ICMA was nominated as an observer on the HLEG and was represented by Nicholas Pfaff. The HLEG report aims to provide the EU with a roadmap for developing a comprehensive sustainable finance policy. It makes a number of key recommendations, including:

- a classification system, or "taxonomy", to provide market clarity on what is "sustainable";
- clarification of the duties of investors' when it comes to achieving a more sustainable financial system;
- an improvement in disclosure by financial institutions and companies on how sustainability is factored into their decision-making;
- an EU-wide label for green investment funds;
- making sustainability part of the mandates of the European Supervisory Authorities (ESAs);
- a European standard for green bonds.

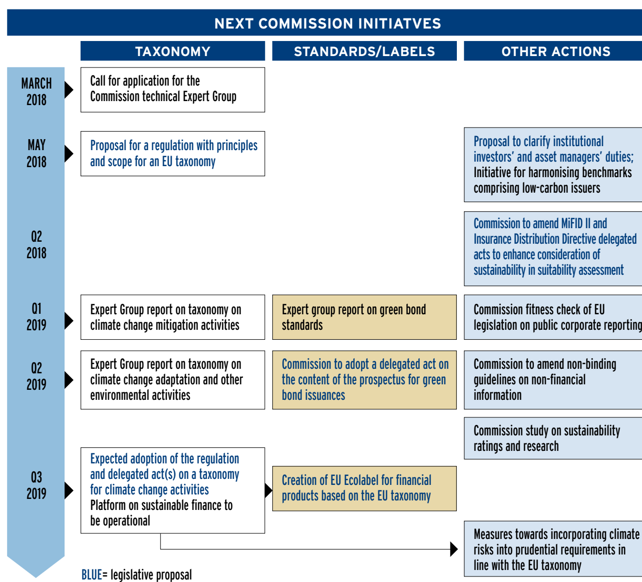
The Commission subsequently released on 8 March an Action Plan on sustainable finance that follows many of the HLEG's recommendations. The Action Plan identifies 10 priorities:

1. Better integrating sustainability in ratings and market research
2. Clarifying institutional investors' and asset managers' duties
3. Incorporating sustainability in prudential requirements
4. Strengthening sustainability disclosure and accounting rule-making
5. Fostering sustainable corporate governance and attenuating short-termism in capital markets
6. Establishing an EU classification system for sustainable activities
7. Creating Standards and labels for green financial products
8. Fostering investment in sustainable projects
9. Incorporating sustainability when providing financial advice
10. Developing sustainability benchmarks

ICMA has expressed support for the Action Plan, noting its breadth and ambition in promoting the transition to a sustainable economy. Certain proposals may however need adjustment to avoid creating unintended barriers to market development. The key challenge with the Action Plan will be to find the right balance in implementation, and not create regulatory complexity or legal uncertainty as the ultimate goal is to increase investment and finance for sustainable projects.

ICMA contributed to the HLEG among others on the proposals aimed at the green bond market such as an EU Green Bond Standard and a possible future label, while also underlining the success of the current voluntary and self-regulatory nature of the international green bond market. ICMA otherwise contributed to the discussion on investor duties and expressed concern on direct legislative action rather than alternative forms of guidance to clarify institutional investors' duties in relation to sustainability issues.

Figure 1: Calendar of the European Commission Action Plan on Sustainable Finance



Generally, the Commission is proposing in the Action Plan a number of legislative initiatives by end-2019 (see calendar in Figure 1). Some of these could potentially lead to unintended complexity and consequences for market participants. Specifically, among others:

- For investor duties "the Commission will table a legislative proposal to clarify institutional investors' and asset managers' duties in relation to sustainability considerations by Q2 2018. The proposal will aim to (i) explicitly require institutional investors and asset managers to integrate sustainability considerations in the investment decision-making process, and (ii) increase transparency towards end-investors on how they integrate such sustainability factors in their investment decisions, in particular as concerns their exposure to sustainability risks."
- For suitability assessments, "the Commission will amend the MiFID II and IDD delegated acts in Q2 2018 to ensure that sustainability preferences are taken into account in the suitability assessment. Based on these delegated acts, the Commission will invite the European Securities Markets Authority (ESMA) to include provisions on sustainability preferences in its guidelines on the suitability assessment to be updated by Q4 2018."
- For green bond issues, the Commission will "specify by Q2 2019 the content of the prospectus for green bond issuances".

On the last point for green bond prospectuses, it is important to underline that any content requirements for issuers leading to explicit or implicit undertakings on actual environmental project impact or performance should be avoided. They could indeed generate potential liabilities for issuers on outcomes that they may not have the capacity to commit to.

The Commission's Action Plan otherwise addresses the question of how the prudential framework may need to further account for the development of green finance, especially as it mitigates climate risk, as well as possibly incentivise its growth (eg through a "green supporting factor"). The Commission will indeed "explore the feasibility of the inclusion of risks associated with climate and other environmental factors in institutions' risk management policies and the potential calibration of capital requirements of banks as part of the Capital Requirement Regulation and Directive".

It is important to note that the follow-up dialogue between the Commission and the market on its Action Plan will take place via a Technical Expert Group on sustainable finance for which ICMA will submit is candidacy. The Expert Group will assist the Commission, notably in the development of:

1. an EU taxonomy or classification system of climate change mitigation, climate change adaptation and other environmental activities;
2. an EU Green Bond Standard;
3. a category of "low carbon" indices for use by asset and portfolio managers as a benchmark for a low carbon investment strategy; and
4. metrics allowing improving disclosure on climate-related information.

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ESRB Recommendation on liquidity and leverage risks in investment funds

By Stéphane Janin

On 14 February 2018, the European Systemic Risk Board (ESRB) published a Recommendation on liquidity and leverage risks in investment funds (ESRB/2017/6), which it had adopted on 7 December 2017. The Recommendation is supplemented by an Annex I "Compliance criteria for the recommendations" and an Annex II "Economic rationale and assessment". The Recommendation contains five policy recommendations addressing liquidity management tools, liquidity mismatches, stress testing, UCITS reporting and leverage limits, directed at either the European Commission to change UCITS Directive and AIFMD legislation or to ESMA to create guidelines for firms and/or to national competent authorities (NCAs).

ESRB proposes significant changes to EU legislation for the fund sector:

- Recommendation A (liquidity risk tools) requires that the Commission change primary legislation to include additional liquidity management tools and to use the power to suspend redemptions;
- Recommendation B (liquidity mismatches) requires the Commission to change primary legislation to mandate ESMA to create a list of "inherently less liquid assets" and subject funds investing in such assets with additional supervisory controls;
- Recommendation C (stress testing) requests ESMA to develop guidance for firms for the stress testing of liquidity risk for individual AIFs and UCITS funds;
- Recommendation D (UCITS reporting) requires the Commission to change legislation in order to require UCITS and UCITS management companies to regularly report data, especially regarding liquidity risk and leverage, to their competent authorities; and
- Recommendation E (leverage limits) requires ESMA to produce guidance on the design, calibration and implementation of leverage limits.

This ESRB report took the European fund industry by surprise.

In terms of process, while the EU fund industry is used to public consultations by the European Supervisory Authorities (ESAs), and by ESMA in particular, there was no consultation by the ESRB.

In terms of content, considering the granularity of the proposed recommendations as developed in the Annexes, this first *ad hoc* public document from the ESRB targeting specifically EU investment funds also raises a question: to what extent, on the ground of macroeconomic risk, can macroprudential supervisors enter the field of microeconomic regulation of financial market players and the scope of action of European and national securities regulators. It is important to remember that currently the voting membership of the ESRB General Board is composed primarily of national central banks, while the official regulators and supervisors for fund managers and investment funds are national securities regulators.

The European institutions are currently debating the official review of ESAs and the improvement of their governance, which includes a review of the ESRB. In this regard, the lack of public consultation, the introduction of macro-risk supervisors into the field of micro-regulation, and the unbalanced composition of the board of the macroprudential supervisor should justify that the ESAs review includes an improvement of the functioning and composition of the ESRB.

As early as 2016 AMIC stressed such concerns in its official response to the European Commission's consultation on the EU macroprudential framework. Two years later, this specific report of the ESRB now illustrates in practice

the risk of unintended consequences due to the current functioning and composition of the ESRB.

In addition, considering the current work carried out by regulators on leverage and liquidity topics at global level, the release of the ESRB's report in February 2018 could be considered premature. In particular, IOSCO is still working on measures to address leverage risk, and its public consultation is expected to be launched in the coming months. This IOSCO initiative, complemented by a recently published report on liquidity risk, responds to the FSB's 2017 policy recommendations to address structural vulnerabilities from asset management activities.

There is therefore a risk that the ESRB's report could undercut international coordination on these issues. Moreover, if it appears that the ESRB's Recommendation to be applied in the EU goes beyond what is required at worldwide level through IOSCO, it would weaken EU-based fund managers facing stricter rules compared to their non-EU competitors. This is even more worrying when some regions are re-examining their own regulatory frameworks in a more pragmatic way (eg see US Treasury report on asset management issued on 26 October 2017).

It should be remembered that the existing EU regulatory framework applicable to EU investment funds and their EU-based fund managers (the UCITS and the AIFM Directives) is already today ahead of the curve at worldwide level in terms of regulatory safety for investors. Furthermore, the AIFM Directive was explicitly initiated by the European Commission to tackle systemic risks related to asset managers and funds, in the context of the regulatory actions launched at worldwide level at that time following the financial crisis.

As no market failure has occurred in Europe in the area of investment funds since the implementation of AIFMD, we do not see the need to now launch a new set of rules while the EU is already a regulatory leader at global level. As the joint AMIC and EFAMA reports on liquidity risk (2016) and leverage (2017) made clear, the UCITS Directive and AIFMD contain a very comprehensive regulatory framework with tools for fund managers and regulators to address risks – including systemic risks.

The AMIC Fund Liquidity Working Group will continue to analyse the detailed proposals in the ESRB report and will engage if necessary with policy makers on specific issues when they are raised. However, we believe in any case that before any new policies are planned to be proposed, formal consultation with industry should be undertaken and that the existing regulatory framework should be sufficiently taken into account.

Stéphane Janin *is Head of Global Regulatory Development, AXA Investment Managers, Vice-Chair of AMIC and Chair of the AMIC Working Group on Fund Liquidity.*

Before any new policies are proposed, formal consultation with industry should be undertaken and the existing regulatory framework should be sufficiently taken into account.

Private placement study on market and regulatory obstacles

By Katie Kelly

US private placements, Schuldschein and, more recently, euro private placement in France have developed successfully into credible, functioning private placement markets, and a renewed, pan-European impetus to reduce over-reliance on bank funding, to complement other funding instruments and diversify funding sources has led to the development of private placement markets elsewhere. In line with Capital Markets Union, a pan-European private placement solution should help to mobilise capital and channel it to where it is most needed, deepen financial integration, increase the stability of the financial system and enhance European competitiveness.

With a view to encouraging the development of this market, the European Commission recently commissioned a study on *Identifying Market and Regulatory Obstacles to the Development of Private Placement of Debt in the EU*. Undertaken by Linklaters and Boston Consulting Group (BCG), the study sets out to identify and explore any particular legal, regulatory and market barriers to entry to the private placement market, by reference to the well-functioning American, German and French markets.

Private placements are a complementary alternative to public bond markets, and their advantages are well-documented: they do not subject the issuing company to stringent, ongoing disclosure obligations; they have simpler documentation requirements; and, according to interviews conducted by BCG in the study, most issuers are satisfied with the pricing they receive in the private placement markets. With no minimum issue size (other than in certain jurisdictions for withholding tax purposes), issuers can match immediate funding requirements more precisely, thereby limiting the cost of negative carry. No external rating is required, which is especially attractive for small-mid-sized companies which do not necessarily want to go to the expense of obtaining and maintaining a rating. For investors, it leads to portfolio diversification, and an opportunity to build up a relationship with the issuer. Relatively long maturities (compared to public bonds) suit investors' long-term liabilities, and the fact that private placements are mainly buy-to-hold investments means that there is no mark-to-market valuation for accounting purposes, while the resulting illiquidity premium leads to attractive yields and spreads.

Fortuitously therefore, the study identifies no new insurmountable legal, regulatory or market barriers to entry, with those which were unearthed having already been highlighted by the ICMA-led Euro Corporate Debt Private Placement Joint Committee (ECPP JC). The key message from participants in the study is that they are generally content with the current regulatory environment under which private placements operate and that, to the extent possible, they would like to limit any further regulatory interventions affecting this market.

However, issues which *have been* identified include a lack of capacity to conduct in-house analysis and monitor credit worthiness on an ongoing basis, which coupled with a lack of information on target issuers can lead to potentially high costs when deploying additional efforts to conduct credit analysis in these circumstances. A potential solution to this conundrum may be in the form of a back-up independent third-party opinion on the credit quality of the issuer (such as that provided by FIBEN (*Fichier bancaire des entreprises*, the Banque de France's credit registry)), a course of action which is proposed by the study.

The risk charges reflecting market volatility in the capital requirements for private placements determined under Solvency II remain an issue for insurance investors, although not a particularly significant one. ICMA on behalf of the ECPP JC has previously stressed that, as private

Private placements are a complementary alternative to public bond markets, and their advantages are well-documented.

placements generally suit a buy-to-hold strategy, the correct metric for Solvency II capital requirements should be default risk (which is very low) rather than market volatility. Coupled with this, however, is the aforementioned issue of credit analysis, which is particularly pertinent for insurance investors who are subject to Solvency II and who have to identify, measure, monitor and report the risk associated with private placement transactions.

A further concern for market participants is whether the market soundings regime under the Market Abuse Regulation (MAR) is applicable to private placements in bond format. A Commission-led consultation on *Building a Proportionate Regulatory Environment to Support SME Listing* in February 2018 touched upon this point, as to which ICMA responded to the effect that discussions between an issuer and investors take place with a view to establishing that an investor is interested in a proposed transaction, after which any further communications are not for the purposes of *gauging interest* (as is required by the relevant provision in MAR), but rather for the purpose of executing the transaction, and therefore that the soundings regime does not apply to private placements.

For the target issuers, these discussions may be the only available channel to access investors, as to which ICMA does not consider that the spirit of the soundings regime is intended to apply. Of course, for larger, public issuers, the soundings regime can be used as a means to minimise leveraging investors in order to maximise the transaction itself in terms of, for instance, pricing, size and tenor. Were the soundings regime to be applicable to private placements however, the consequences (intended or otherwise) could prove to be a significant detrimental factor for the development of the private placement market due to the obligations imposed on the persons receiving market soundings, which could disincentivise investors and set European private placements at a disadvantage.

Looking forward, the study identifies a number of innovations in the private placement space, such as in product offerings, including private placement funds and green private placements. There have been developments in private placement platforms, which enable users to access, among other things: automated search, filter and match options; automated calculations; anonymous sharing and collection of information; online negotiation of deal terms and online access to termsheets and standardised documentation. Some platforms also offer support with the issuance process, professional risk analysis and comparison of borrowing curves with peers. A further innovation is the use of blockchain, with Daimler AG and Telefonica Deutschland Holding AG recently having successfully used blockchain technology for Schuldschein transactions. Blockchain has great potential to simplify and increase efficiency in financial services, although according to the European Commission's FinTech Action Plan, there remains a lack of certainty and guidance on how to use it, as well as fragmentation and a lack of common approaches between national regulators and supervisors; something which the FinTech Action Plan aims to address.

Finally, the study has identified significant growth potential for private placement in a number of markets, including Austria, Belgium, Denmark, Italy, Ireland, the Netherlands, Poland, Spain, Sweden and the UK. While resolution of the issues set out above or technological advancements could collectively help to develop the private placement market, a more fundamental issue has been identified by the study, being that information and education campaigns should be launched to increase the awareness of private placements among potential issuers and investors and support further market participation across Europe.

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Industry codes of conduct

By Charlotte Bellamy

On 5 February 2018, ICMA submitted a response to the UK FCA's consultation paper on industry-written codes of conduct relating to unregulated markets and activities.

Among other things, the consultation paper sought feedback on proposals for the FCA to recognise particular industry codes that it considers set out proper standards of market conduct for unregulated markets and activities. This means that the FCA would review and assess industry codes related to unregulated markets and activities against new criteria, and state publicly that it considers a particular code is a helpful explanation of the proper standards of market conduct for a particular unregulated market or activity.

ICMA's response outlined the reasons that ICMA believes that the proposals would not apply to its codes, including the ICMA Primary Market Handbook, the ICMA Secondary Market Rules & Recommendations, the ICMA ERCC Guide to Best Practice in the European Repo Market and various other ICMA guides and codes. Primarily, this is because ICMA's guides and codes all relate to regulated market activity, whilst the FCA's proposals relate to unregulated markets and activities. ICMA's codes relate to bond issuance, private placement, bond underwriting, bond trading, repo and cross-border private banking, all of which are subject to a number of UK and European legislative provisions and regimes.

Moreover, the proposed criteria for the FCA to recognise a code would mean that many of ICMA's codes would not be suitable for FCA recognition in any event. For example, the FCA proposals envisage that any recognised code would need to have been subject to public scrutiny and be made publicly available and free for all parties who wish to use it. These requirements are sensible, because firms will need to be able to scrutinise and access industry codes that are recognised by the FCA if they are to comply with them. While certain items of ICMA's codes are publicly available, others are only available to ICMA members and subscribers. Also, ICMA's codes are periodically reviewed and updated (sometimes more than once per year) following engagement with relevant stakeholders, but ICMA generally does not open consultations on updates to ICMA codes to members of the public.

Aside from the key point that the FCA's proposals would not appear to be relevant to ICMA's codes, ICMA raised some general questions and considerations that the FCA may wish to consider in progressing their proposals. These largely related to questions around the scope and practical implications of the proposals for FCA authorised firms.

We understand that the FCA's intention is to publish a policy statement outlining any FCA Handbook changes as a result of this consultation in Q2 2018.

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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 *Public sector issuers:* The Public Sector Issuer Forum met in The Hague on 13 March to discuss: sustainable finance; counterparty risk; MiFID II/R implementation; and international benchmark reform.

2 *MiFID II/R implementation in primary markets:* Taking account of the implementation of MiFID II/R and PRIIPs at the beginning of 2018, ICMA has continued to work with the ICMA Primary Market Practices Committee and the Legal & Documentation Committee on the implications for the primary markets of the MiFID II/R regime for product governance, justification for allocations, and inducements, and the PRIIPs regime, following the circulation of ICMA papers relating to the PRIIPs and MiFID II product governance regime in December 2017 and a paper relating to the MiFID II product governance regime and ECP issuance in February 2018.

3 *Transition from IBORs to risk-free rates:* ICMA's work on the transition from IBORs to risk-free rates is summarised in a box below.

4 *Prospectus Regulation:* ICMA responded on 8 March to ESMA's consultation paper on draft Regulatory Technical Standards under the new Prospectus Regulation, making technical comments on the proposals relating to key financial information for the prospectus summary, data and machine readability of prospectuses, advertisements, prospectus supplements and prospectus publication. A key concern is the prescriptive nature of the proposals on key financial information in the summary.

5 *Private placements:* ICMA responded on 22 February to the European Commission's consultation on *Building a Proportionate Regulatory Environment to Support SME Listing.* The response was limited to the applicability of the MAR soundings regime to private placements.

6 *FCA industry codes of conduct:* ICMA has responded to the FCA consultation on industry codes of conduct, noting that it does not expect the proposals to relate to ICMA codes of conduct, but also highlighting some issues that the FCA may wish to consider further in relation to the proposals.

7 *Bank of Italy requirements:* ICMA continues to liaise with the Bank of Italy in relation to members' continuing queries and concerns on Article 129 reporting rules. With the support of its lead manager constituency and a leading international law firm, ICMA also supported a letter to the Bank of Italy raising concerns with Italian licence requirements for certain issuers placing securities in Italy.

8 *ECP and LCR:* ICMA has responded to the European Commission consultation on amendments to the Liquidity Coverage Ratio (LCR) Delegated Regulation. The ICMA response underscores the ICMA ECP Committee's support for AFME's comments concerning the LCR treatment of ABCP.

9 *ECP and DLT:* Building on distributed ledge technology (DLT), which has been developed in collaboration with ING, ABN and KBC, Commerzbank executed a proof of concept transaction, issuing an ECP for KfW with MEAG as the investor in 2017. A demonstration was subsequently arranged for the ICMA ECP Committee, illustrating how DLT could conceptually be utilised to create a more streamlined process for the issuance and redemption of ECP.

Secondary markets

10 *MiFID II/R regional workshops:* Following a series of ICMA workshops in the autumn of 2017 on the implications of MiFID II/R for fixed income trading, ICMA held post-implementation workshops during the first quarter of 2018 in London and Vienna, Hong Kong and Singapore. Further workshops are planned.

11 *ICMA SMR&R:* ICMA is consulting members on the impact of MiFID II/R and other proposed new EU regulations on the ICMA Secondary Market Rules & Recommendations (SMR&R).

12 *Electronic Trading Council:* The Electronic Trading Working Group and Platform Working Group are being combined to form the Electronic Trading Council (ETC), a technical working group under the umbrella of the ICMA Secondary Market Practices Committee. The ETC will focus on electronic trading and the role of technology in the evolving structure of fixed income secondary markets.

13 *Single name CDS study:* The ICMA study by Andy Hill and Gabriel Callsen into the state and evolution of the European single name credit default swap market, drawing on ISDA data, was launched on 15 February.

14 *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. A separate report is due to be published in the second quarter.

Repo and collateral markets

15 *Year-end repo study:* Following dislocation in the repo market at year-end 2016, ICMA published a report by Andy Hill on the European repo market at year-end 2017, based on market data and interviews with market participants. The 2017 data show that, while there were significant year-end effects on repo rates and on liquidity, these were markedly less severe than in the previous year.

16 *Repo market survey:* ICMA has published its 34th semi-annual survey of the European repo market, reporting on outstanding business as at close of business on 6 December 2017. Overall,

this latest survey shows signs that the repo market is adapting to the new regulatory environment, with the baseline figure being the largest ever recorded by the survey since it began in 2001.

17 *ICMA ERCC AGM:* The ICMA ERCC AGM was held in London on 14 March, featuring sessions outlining the ERCC's recent work, including on the evolution of the GMRA, and a panel discussion on *Unlocking the Value of T2S*.

18 *Guide to Best Practice:* An updated version of the ICMA European Repo and Collateral Council (ERCC) *Guide to Best Practice in the European Repo Market* was published with effect from 18 December 2017. This latest revision reflects changes agreed to date, but work is continuing, and further changes can be expected during 2018.

19 *ERCC Committee composition:* Following the annual election completed in early February, the composition of the ERCC Committee is more diverse than ever, with successful candidates including those from four buy-side firms – AXA IM, BlackRock, PGGM and Swiss Re – and, for the first time ever, a CCP treasury – LCH. The ERCC Committee met in its new composition on 21 February.

20 *SFTR implementation:* ICMA is continuing to help members to implement the EU Securities Financing Transaction Regulation (SFTR), through the ERCC SFTR Task Force.

21 *CCPs:* The ICMA ERCC responded on 28 February to ESMA's consultation on EMIR anti-procyclicality provisions for CCPs. The response flags the importance of European repo and collateral markets in the context of CCP clearing; and it argues that great care needs to be taken fully to assess the way in which such anti-procyclicality measures are calibrated.

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

23 *FinTech mapping:* ICMA's FinTech mapping study, which includes around 100 technology solutions for collateral management and ancillary services, is being kept up-to-date on the ICMA website.

Asset management

24 *AMIC Excom:* At the ICMA Asset Management and Investors Council (AMIC) Executive Committee meeting on 28 February, the FCA made a presentation and answered questions from members on its recent *Asset Management Market Study*.

25 *Bail-in:* The ICMA Bail-In Working Group held a workshop in Frankfurt on 28 February, led by Tim Skeet, at which the ECB was a speaker.

26 *AMIC Council:* The biannual ICMA Asset Management and Investors Council, chaired by Bob Parker, was held at BNP Paribas Fortis in Brussels on 6 March. Commissioner Katainen was a keynote speaker. Panels at the Council covered: smart beta; corporate governance; and illiquid versus liquid investments.

27 *Fund delegation:* The AMIC Executive Committee has approved the launch of a stand-alone AMIC position paper on fund delegation to emphasise the importance of the current fund delegation model to the European asset management industry.

28 *Fund liquidity:* The European Systemic Risk Board adopted a recommendation on liquidity and leverage risks in investment funds on 7 December, and IOSCO issued recommendations on liquidity risk management in open-ended collective investment schemes on 1 February 2018. Both of these recommendations are being assessed in the AMIC Fund Liquidity Working Group.

29 *Corporate governance:* The AMIC Corporate Governance Working Group, chaired by Georg Grodzki, has responded to the Financial Reporting Council's consultation on revising the UK Corporate Governance Code and on changing the Stewardship Code.

Green, social and sustainable bond markets

30 *European Commission High Level Expert Group (HLEG) on Sustainable Finance:* The HLEG published its final report on 31 January, including recommendations for an EU Green Bond Standard and a Sustainability Taxonomy. ICMA was represented on the HLEG by Nicholas Pfaff as an observer.

31 *European Commission Action Plan on sustainable finance:* The Commission's Action Plan, published on 8 March, follows many of the HLEG's recommendations, including an EU Green Bond Standard and a Sustainability Taxonomy, as well as greater emphasis on sustainability as part of investor duties. A study will also review possible prudential adjustments related to climate change risks. The Commission has called for candidacies for a Technical Expert Group on sustainable finance to be submitted by 16 April.

32 *France's Green Evaluation Council:* ICMA has been nominated as an observer on the Evaluation Council of France's green sovereign bond and will be represented by Nicholas Pfaff. The Evaluation Council will define the specifications and schedule for evaluation reports on the environmental impact of France's green sovereign bond.

Other meetings with central banks and regulators

33 *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.

34 *ICMA Regulatory Policy Committee:* Edwin Schooling Latter, Head of Markets at the FCA, joined the ICMA Regulatory Policy Committee on 15 March for a discussion on regulatory developments.

35 *ICMA Capital Market Lecture:* Andrew Bailey, Chief Executive of the FCA, gave a Capital Market Lecture, which ICMA organised jointly with AFME and ISDA, at NatWest Markets on 1 March on *Recent Developments in Financial Markets*.

36 *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.

Note: An updated draft of the *ICMA Regulatory Grid* has been posted on a password-protected webpage on the ICMA website.

The transition from IBORs to near risk-free rates

This box summarises ICMA's involvement in work on the transition from IBORs (eg LIBOR) to near risk-free rates (RFRs). ICMA is involved in a number of different and complementary ways:

Sterling RFRs

2 First, in the UK, where SONIA has been chosen as the preferred RFR, the remit of the Sterling RFR Working Group has been broadened from the derivatives market to include the cash markets, including the loan market and the bond market. ICMA has been asked by the Bank of England and the FCA, and agreed, to chair a new Bond Market Sub-Group, whose remit relates to the transition from LIBOR to RFRs in the sterling bond market, including FRNs, securitisations and capital securities.

3 With the Bank of England and the FCA, ICMA has established a Bond Market Sub-Group which is designed to be representative of the sterling bond market as a whole, and comprises: public sector, corporate sector and financial sector issuers; asset managers and investors; financial intermediaries in the primary and secondary markets; four of the most active law firms in the bond market; trade associations with a particular interest in the sterling bond market; and the Bank of England/FCA, who provide the Secretariat.

4 The first meeting of the Bond Market Sub-Group, chaired by Paul Richards, was held at the FCA on 16 February, and a subsequent meeting on 26 March. On each occasion, there was a high turnout. The issues being addressed include: how the transition from LIBOR to SONIA should be managed in the sterling bond market; whether it is feasible to convert legacy bonds from LIBOR to SONIA and if so how, bearing in mind that protocols are not currently used in the cash markets; a set of other legal issues; coordination between the cash and derivatives markets and between the UK and other IBOR jurisdictions; and raising awareness of the transition to risk-free rates.

Euro and Swiss franc RFRs

5 Second, ICMA has been invited, and agreed, to join the Euro RFR Working Group, organised by the ECB, the European Commission, ESMA and FSMA (the Belgian regulator). The main task of the Euro RFR Working Group is to choose an RFR for the euro, though additional workstreams are being established: in particular to address questions relating to term structure and contractual robustness. The main members of the Working Group are banks. ICMA, represented by David Hiscock, is a non-voting member of the Working Group, along with a few other trade associations.

6 ICMA has also been invited, and agreed, to join the National Working Group on Swiss Franc Reference Rates (NWG), co-chaired by the Swiss National Bank and ZKB. Martin Scheck will be representing ICMA on the NWG. Beat Gabathuler, from ZKB, chair of the ICMA Swiss Regional Committee, is already a member of the NWG.

Global benchmark survey

7 Third, ICMA has been invited by ISDA, and agreed, to support a global benchmark survey, along with SIFMA, SIFMA Asset Management Group and AFME. The detailed work on the survey is being carried out by Ernst & Young (EY). A roadmap was published on 1 February. In-person interviews have been conducted by EY, and an electronic survey has also been organised by EY. A report is due to be prepared by EY by the summer summarising the results of the survey. The authorities in the five main IBOR jurisdictions – ie the UK, the US, the euro area, Switzerland and Japan – are being consulted at each stage in the process.

Awareness raising

8 Fourth, the authorities are keen to raise awareness of the transition to RFRs in the cash markets. ICMA has been asked to help. The FCA has attended a number of ICMA Committees to discuss the transition to RFRs; and ICMA is arranging a panel on international benchmark reform, with officials from different IBOR jurisdictions, at the Conference after the ICMA AGM in Madrid at the end of May.

9 ICMA also published a Quarterly Assessment on *The Transition from LIBOR* (in the ICMA Quarterly Report for the First Quarter of 2018); and joined a number of other trade associations in a letter dated 31 January to the Financial Stability Board on issues to be considered in the transition from LIBOR to RFRs globally in the cash markets.

ICMA webpage

10 Finally, ICMA has set up a benchmark reform webpage, which covers: ICMA's own recent work on RFRs; publicly available official documents on benchmark reform from the authorities in the five main IBOR jurisdictions; joint work involving ICMA and other trade associations; and links to earlier work by ICMA.

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Primary Markets

by Ruari Ewing and Charlotte Bellamy

PRIIPs and MiFID II product governance: the initial experience

Since the beginning of the year, various ICMA members have reportedly been using the ICMA1 ("all bonds"/"professionals only") and ICMA2 ("simple listed bonds"/"general retail") approaches to the PRIIPs and MiFID II product governance (PG) regimes. These were outlined in, respectively, the 2017 Q4 and 2018 Q1 editions of this Quarterly Report.

Various ICMA working group deliberations continue, however, as: (i) the most directly affected market players (the more active "manufacturers" and "distributors") continue to deepen and widen their initial understanding of the regimes (including more marginal scenarios) and explore potential new compliance approaches; and (ii) other stakeholders (less active manufacturers/distributors, more geographically remote intermediaries, other borrowers, related advisors, investors and also regulators) familiarise themselves and react to "manufacturer"/"distributor" approaches. In this respect, ICMA staff presentations recapping on current dynamics have been published on ICMA's *MiFID II/R in primary markets* webpage.

There was significant press coverage in the major UK financial press at the start of the year concerning PRIIPs key information documents (KIDs) allegedly produced according the officially prescribed methodologies yet presenting results so extreme as to be misleading. The UK FCA subsequently acknowledged that, for some PRIIPs, "the 'performance scenario' information required in the KID may appear too optimistic and so has the potential to mislead consumers" and that reasons for this may include "the way the calculations in the RTSs must be carried out". The FCA noted in this respect being comfortable with manufacturers that produce KIDs "provide explanatory materials" to provide context and set out their concerns. But query then additional space sufficiency within the KID's strictly limited three pages and any "disclosure chain" considerations (the KID has to be a standalone document albeit with a strictly defined allowance for cross-references). ESMA's Chair, Steven Maijoor, has recently stated that ESMA is working on further guidance, on performance scenarios-related issues in particular. However, none of this seems likely to encourage, at least for now, benchmark borrowers who can access the institutional markets to produce KIDs (having set their likely focus on certainty of funding against liability considerations in the context of these large funding exposures running into the billions).

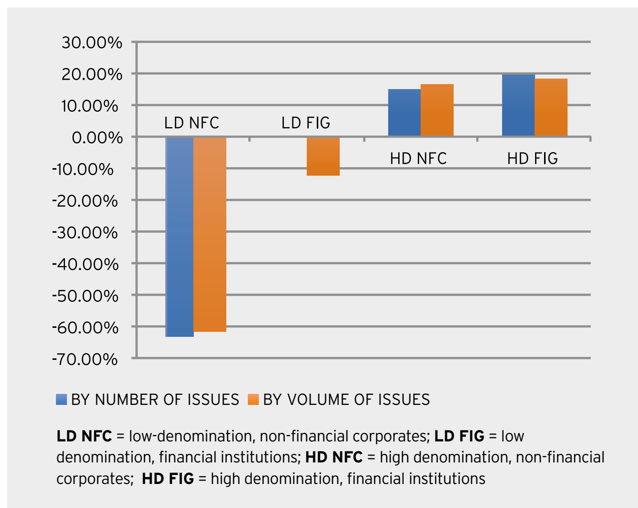
And it is distinctly worth remembering that prior PRIIPs coverage in this Quarterly Report noted potential liability concerns stemming from the PRIIPs KID concept itself (irrespective of the officially prescribed methodologies), starting with the KID's vague purpose – which a speech by ESMA's Chair, Steven Maijoor, interpreted as being *inter alia* to "contain sufficient information to allow consumers to make an informed investment decision". This seems close to the Prospectus Directive test for a full prospectus ("all information [...] necessary to enable investors to make an informed assessment"). It seems challenging, in a €500 million - €2 billion context, to reconcile discharging such a fulsome disclosure test in the KID's three pages, particularly set against the PRIIPs Regulation's absolute prohibition on the KID being "misleading." There is also the specific obligation that the KID include "key" information specified as such under the Regulation: the Regulation's civil liability exemption (for KIDs that are accurate, non-misleading and otherwise consistent with other specified documents such as a prospectus) would not apply to any consequential civil liability claim arising under non-EEA laws such as in the US (an important consideration given the international nature of the bond markets).

ICMA has conducted an initial analysis of Dealogic's new issue data for indications of any new regime impact on the availability of vanilla bonds to general retail investors. It did so by comparing the prevalence of low (€1,000 or less) and high (€100,000 or more) denominations in euro new issue data for 2018 Q1 (as of 21 March) against the equivalent 2017

Q1 data (the single currency scope limitation being to simplify the analysis). Given the many possible types of debt securities (involving different combinations of features) that have evolved to meet borrower and investor needs, there is no exhaustive and authoritative bond type nomenclature. ICMA's analysis consequentially focused on benchmark issuance (aggregate issue sizes of €500 million or more) as a rough proxy for vanilla bonds, since the only other bonds of that size are likely to be asset/mortgage-backed bonds that can be controlled for in Dealogic's nomenclature. Lastly, bonds have not traditionally had generic formal "retail" designations (having rather various retail-like characteristics stemming from regulatory, commercial or other drivers). ICMA's analysis consequentially focused on denomination as a rough proxy for potential retail status. Many bonds have €100,000 denominations, meaning that they can only be bought or sold in sizes of at least that order of magnitude (the trading value of vanilla bonds tends to oscillate around 100% of the denomination's face value – absent default or similar concerns). However general retail investors will only plausibly buy bonds with denominations of around €100, €1,000 or perhaps €10,000.

The analysis[1] by number and value of issuances, as shown in the chart below, reveals a marked decrease in low denomination issuances (over 60% in the case of non-financial corporate bonds), in contrast to 15%-20% increases in high denomination issuances.[2]

Percentage change in issuance 2018 Q1 over 2017 Q1



Source: Dealogic

It remains to be confirmed whether this very significant reduction in vanilla low denomination bonds (i) indicates an ongoing trend, (ii) is caused by the PRIIPs and/or PG regimes and/or (iii) will be a concern for European authorities (eg in the context of the EU's CMU objectives). These initial results give food for thought in any case. A simpler statistic yet may be found in the number of KIDs known by ICMA to have been prepared among all benchmark bonds (not just the above EUR data set) since the PRIIPs regime took effect: none so far.

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Prospectus Regulation: draft RTS

On 8 March 2018, ICMA submitted its response to *ESMA's Consultation Paper on Draft RTS under the New Prospectus Regulation*.

The consultation paper covered five distinct areas for which ESMA is mandated to deliver draft RTS to the European Commission, namely key financial information for the prospectus summary, data and machine readability of prospectuses, advertisements, prospectus supplements and prospectus publication.

Key financial information in the prospectus summary

ESMA has proposed a relatively prescriptive approach for the inclusion of key financial information in the prospectus summary, setting out a limited number of tables for broad categories of issuers which mandate certain financial statement line items to be included in the prospectus summary. A degree of flexibility is envisaged through (i) requiring certain line items only where they have been disclosed elsewhere in the prospectus, and (ii) the ability for the issuer to include up to three additional line items or alternative performance measures (APMs) in the summary.

ICMA has raised concerns with the proposed approach, noting that prescriptive requirements can give rise to unexpected results in practice when they are applied to the wide range of prospectuses prepared under the EU prospectus regime. This introduces increased costs for issuers, who need to spend time understanding how best to comply with prescriptive requirements that do not necessarily fit with their business.

1. This analysis involved a data set of 953 bond issues worth €882.7 billion, roughly equally split between the first quarters of 2018 (as of 21 March) and 2017. Around a quarter of the issues did not have denomination data and were discarded, leaving 698 issues worth €694.9 billion to analyse (again roughly equally split between the two first quarters). Aside from two issues only with €50,000 denominations, all issue denominations were relatively polarised between low denominations (€1,000 or less) and high denominations (€100,000 or more). 38 asset/mortgage-backed bonds were excluded (as non-vanilla), as were 160 sovereign, supranational and agency (SSA) bonds (as significantly less impacted or even exempt from the new regimes) – thus leaving 498 bonds worth €393 billion from financial institution and non-financial corporate borrowers most likely to be impacted (in a ratio of around 6/4).

2. The excluded SSA issuances decreased generally, though more markedly in high denominations.

To ameliorate this concern, ICMA has encouraged ESMA to remove the proposed cap on the number of additional line items or APMs that can be included in the summary (to the extent the prescriptive annexes to the proposed draft RTS are retained).

Separately, ESMA's proposals in relation to APM disclosure in the summary are not yet clear. For example, ESMA refers to issuers using footnotes to explain APMs where necessary, but it is not clear if that approach is mandatory or not.

Data and machine readability

ESMA has proposed a very detailed set of data to be reported by national competent authorities (NCAs) to ESMA. Furthermore, ESMA has proposed that NCAs would be able to ask issuers to report that information to the NCA.

It appears that the submission of data to ESMA has two purposes: (i) to allow ESMA to compile its report on prospectuses in accordance with Prospectus Regulation Article 47 which seems to be intended to facilitate regulatory oversight of prospectuses and issuance within the scope of the Prospectus Regulation; and (ii) to allow investors to search for prospectuses published under the Prospectus Regulation.

While purpose (i) is unobjectionable, the data that ESMA requires should be kept to a minimum to avoid any unnecessary cost and administrative burdens on NCAs and market participants.

Purpose (ii) is envisaged in Prospectus Regulation Article 21(6) and Recital 63, and the general principle of facilitating investor access to documents published under the Prospectus Regulation is understandable. However, from an investor protection perspective, it seems important that the updated Prospectus Register does not develop into more than a simple tool allowing investors to search and access documents published under the Prospectus Regulation, for example by giving information on securities outside of the published documents and/or allowing investors to compare different securities without looking at the relevant prospectuses. ICMA has encouraged ESMA to avoid this pitfall through both the design of the updated Prospectus Register and also by minimising the information that is available to the public in the database.

ICMA has therefore suggested that ESMA keeps the data required to a minimum (including removing certain of the data items which do not seem strictly necessary for ESMA to fulfil its obligations under Level 1).

Separately, it is important that ESMA does not push the reporting burden from NCAs on to issuers. This will increase costs and administrative burdens for issuers, which is not in line with the general legislative intent of the Prospectus Regulation. It would also result in a doubling up of compliance costs and administrative burden, with the issuer providing the information to the NCA and the NCA then needing to check the information provided to it by the issuer in order to ensure it is providing correct information to ESMA. Also, given the information required is relatively straightforward and, in many cases, better known by the NCA than the issuer, it is unclear why issuers should be required to provide this information to NCAs.

Advertisements

ESMA has carried across certain existing Prospectus Directive (PD) Level 2 provisions relating to advertisements. It has also suggested some new requirements which largely relate to the content and warnings contained in advertisements.

Unfortunately, ICMA's concerns with the Level 1 definition of advertisement were not taken on board by the co-legislators when the Prospectus Regulation was being finalised, meaning that the definition of "advertisement" under the Prospectus Regulation could potentially capture a wide range of oral and written "communications" (rather than "announcements", which was the term used in the PD). In light of this wide definition, some of ESMA's proposals may be problematic in practice.

In its consultation paper, ESMA provides some examples of the types of communication that it considers to be captured by the new definition of advertisement. The examples appear to be helpful and generally in line with the concept of a communication that is widely disseminated (regardless of whether each individual communication is bilateral or not), rather than a bespoke or specific bilateral communication that might happen on a one-off basis.

However, even with this helpful list of examples, concerns remain in relation to how certain elements of the proposed draft RTS will apply in practice. The ICMA response outlines those concerns and gives practical examples of the problems that could arise in practice. As a result of this, ICMA has encouraged ESMA to restrict the proposed new requirements to written advertisements only, and suggested certain other technical changes to the proposed draft RTS.

ICMA is also discussing the potential impact of the broadened definition of the term "advertisement" under the Prospectus Regulation with members.

Supplements

ESMA has largely carried across existing PD Level 2 provisions relating to circumstances that require a prospectus supplement, which is helpful. While ICMA's general view remains per the ICMA 2013 response to the *PD II Consultation on Supplements* (ie it should be for issuers to decide whether a specific situation meets the test for publishing a supplement and it is not necessary for legislation to prescribe specific instances of when a supplement is required), market participants are now familiar with these requirements and so retaining them will avoid additional costs for issuers in

analysing and understanding any new provisions with their legal advisers.

ICMA's response also reiterates the point made in the ICMA 2017 response on *Format and Content of the Prospectus* that a profit forecast should not be mandatory for prospectuses related to non-equity securities, and so the additional supplement trigger proposed by ESMA should not be relevant for the majority of non-equity prospectuses.

Publication

ESMA proposes to carry across relevant provisions from the current PD Level 2 measures, which is a helpful approach and will minimise additional costs for issuers.

Next steps

The deadline for ESMA to deliver its final report with draft RTS on the topics covered in this consultation is 21 July 2018.

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Prospectus Regulation: other aspects

ESMA published its *Final Report on Technical Advice under the Prospectus Regulation* covering format and content of the prospectus, format and content of the EU Growth Prospectus and scrutiny and approval of the prospectus on 3 April 2018. ICMA previously responded to the consultations on *Format and Content of the Prospectus* and *Scrutiny and Approval of the Prospectus* in September 2017.

ESMA's technical advice has been delivered to the European Commission for consideration and is expected to form the basis for the bulk of the Level 2 provisions under the Prospectus Regulation, which will take the form of Commission delegated acts. In terms of timing, the indicative timetable set out in the Commission's request to ESMA for technical advice (reproduced at page 252 of ESMA's Final Report) indicates that:

- the Commission will prepare draft delegated acts on the basis of ESMA's technical advice by June 2018;
- the draft delegated acts will be translated and adopted by October 2018;
- the European Parliament and the Council will have an objection period until April 2019; and
- the date of application of the Prospectus Regulation and delegated acts will be 21 July 2019.

ICMA will carefully consider the impact of ESMA's final report with interested members. One immediate point to note is that, helpfully, it appears that the proposal to mandate disclosure of profit forecasts and profit estimates will not be taken forward for debt prospectuses, with ESMA stating at para 129 of the final report: "ESMA is of the view that profit forecasts and profit estimates are not generally deemed to be as important for non-equity (in contrast to equity) investors, and it will not include in its technical advice that outstanding profit forecasts or profit estimates must be reproduced in non-equity prospectuses. Nevertheless, an issuer of non-equity securities must assess whether or not an outstanding profit forecast is material for investors. If so, it must be included in the prospectus in accordance with Article 6 of the PR." This approach is welcome and in line with the ICMA response to the consultation on *Format and Content of the Prospectus*. Less helpfully for issuers, ESMA suggests that a statement on any profit forecast or estimate will still be required, but does not require such statement to be given by auditors. In addition, the Technical Advice includes a three page limit on prospectus cover notes, which may require some changes to current prospectus disclosure.

Also in relation to profit forecasts, ESMA published an updated *Q&A on Prospectuses* including a new question 102 on the definition of profit forecast on 28 March 2018. The Q&A gives guidance and examples of what would and would not be a profit forecast and notes that it is not possible to remove information from the scope of the definition of profit forecast by merely stating that it is not a profit forecast.

In relation to other aspects of the Prospectus Regulation, we are currently expecting:

- a consultation paper on ESMA guidelines on risk factors to be published in mid-July 2018, with the consultation running until early October 2018 and the guidelines to be published in March 2019;
- ESMA to begin working on equivalence criteria for prospectuses drawn up under the laws of third countries (the precise timing for this is currently unclear);
- the majority of provisions under the Prospectus Regulation will apply from 21 July 2019, although certain provisions are already in application or will apply from 21 July 2018.

Separately, the European Commission Action Plan on *Financing Sustainable Growth* published in March 2018 states: "Within the framework of the Prospectus Regulation, the Commission will specify by Q2 2019 the content of the prospectus for green bond issuances to provide potential investors with additional information." ICMA intends to monitor developments on this point. It is hoped that the Commission will not specify overly prescriptive requirements that could raise potential liability concerns for issuers and/or unnecessarily hinder issuance of green and other sustainable bonds.

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Issuer Legal Entity Identifiers

As of 2 April 2018, an issuer Legal Entity Identifier (LEI) code is a mandatory eligibility criterion for new issues in both Clearstream and Euroclear. ICMA understands that the process for obtaining an LEI can take a number of weeks, so issuers who do not yet have an LEI will need to consider the need for an LEI well in advance of closing a new issue. LEIs must also be re-certified annually.

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Asset-Backed Commercial Paper

On 24 January 2018, the European Commission opened a consultation (for comment by 21 February) regarding a new draft Delegated Regulation, amending an existing Commission Delegated Regulation, with regard to the Liquidity Coverage Ratio (LCR). AFME submitted a response to this consultation, focused on the way in which securitisation is treated in the LCR and particularly considering how STS securitisation should be integrated into the existing framework. Given that this included important proposals regarding the LCR treatment of Asset-Backed Commercial Paper (ABCP), ICMA voiced its support for this AFME response.

In brief, ICMA is supportive of the LCR, which represents an important and broadly successful element within the package of financial regulatory reforms enacted in response to the financial crisis. Nevertheless, refining this through a targeted amendment of the LCR Delegated Regulation can further improve the LCR. It also presents a valuable opportunity for integration into the LCR Delegated Regulation of the new STS criteria for securitisation, particularly including for the LCR treatment of ABCP – which is an important financing tool for the real economy.

As reported in this section of Issue no 48 of the ICMA Quarterly Report, on 15 December 2017, the EBA launched two consultation papers on draft technical standards implementing the new EU Securitisation Regulation and then on 19 December, ESMA published three further such consultation papers. AFME responses to four of these consultations were duly submitted. These included a number of points of particular relevance from an ABCP perspective.

ESMA re STS notification:

- Most importantly, the STS notification templates do not appear to contemplate the possibility that an ABCP transaction will be notified as STS in the absence of a corresponding notification that the ABCP programme funding it is also STS. This is a serious omission and its correction is essential, including because this seems to be a clear contradiction of the legislative policy intent. Further, it does not make sense, because the source of the funds for a securitisation does not affect the simplicity, transparency or standardisation of the transaction itself; and, as a practical matter, interpreting the Securitisation Regulation such that ABCP transactions will not be able to be notified as STS separate from the programmes that fund them is likely to cause the STS initiative to fail with respect to the ABCP markets (since most ABCP programme sponsors have currently concluded that it will not be practicable for them to obtain STS designation for their STS programmes).
- The draft RTS fails to reflect that Article 27(1) clearly makes STS notification in respect of ABCP transactions and ABCP programmes the exclusive responsibility of the sponsor.
- There is significant potential for compliance uncertainty raised by the interaction of the definition of an ABCP transaction (a securitisation within an ABCP programme) and the STS notification – since this definition of an ABCP transaction does not contemplate the possibility of a securitisation funded by multiple funders, some or all of which might be ABCP programmes. Where that is the case, multiple STS notifications may need to be given in respect of the same transaction.
- The data suggested in the general information section of Annex II seem reasonable, except that disclosing information relating to the originators of ABCP transactions in the STS notification is not appropriate and is inconsistent with the disclosure regime as it applies to ABCP securitisations.
- The date on which the securities are "deemed" to be issued is confusing. It would seem better to instead refer to the transaction signing date for ABCP transactions and the date of first issuance for ABCP programmes.

ESMA re disclosure requirements, operational standards, and access conditions:

- Both ABCP transactions and ABCP programmes are very often private transactions, so the approach proposed – which is that the reporting templates do not apply to private securitisations – is welcomed.
- Considering the reporting of ABCP underlying exposures where the sponsor is the reporting entity, it should only be necessary to produce transaction-by-transaction data if requested to do so by the competent authority and it should otherwise be provided in aggregate form. Where information is provided in aggregate form, the information should be of a type relevant to all the transactions in an

ABCP programme, so as to ensure it is capable of being understood and read on an aggregate programme-wide basis by investors and potential investors.

- No need is foreseen to extend the templates to cover the possible development of synthetic ABCP securitisations.
- The maximum one-month time between the data cut-off date and the submission date for ABCP securitisations is workable from the point of view of data providers and still useful for investors.

EBA re homogeneity of underlying exposures:

- For ABCP STS securitisation it makes sense to require that the underlying exposures have been underwritten according to similar standards, methods and criteria; are serviced according to uniform servicing procedures; and all fall within the same asset category. But a requirement based on the relevant risk factors applicable in the context of non-ABCP STS securitisations is not appropriate – in the case of an STS ABCP transaction, the only investor with direct exposure to the pool is the sponsor of the transaction who is providing liquidity support (all other investors are primarily exposed to the credit of the sponsor); and the originators of transactions in ABCP transactions will typically be clients of the sponsor institution, whose business plans, risk-profiles and receivables are well-known to the sponsor institution (which will necessarily be a credit institution or investment firm that has completed extensive due diligence and credit underwriting).

EBA re risk retention:

- Underlying transactions in ABCP programmes are examples of certain types of securitisations which do not involve an offering document. In such cases, the proposed clarification that various disclosures relating to the retention commitment should be made via the final offering document or prospectus risks creating confusion and should be removed.

Circulated on 16 February, AFME's *Fourth Quarter 2017 Securitisation Data Report* shows that European ABCP issuance was €67.2 billion in the fourth quarter of 2017. This is an increase of 11.6% versus the prior quarter but represents a decline of 20.3% versus the same quarter in the prior year. Multi-seller conduits (97.4% of total), particularly from France (81.3% of total), continue to dominate as the largest issuance category in the ABCP market. European ABCP issuance for full year 2017 was €293.1 billion, a marked decline of 34.3% versus the prior year total.

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ECP and MiFID II product governance

In February 2018, ICMA circulated a note to ICMA primary market members relating to the status of ECP dealers under MiFID II product governance rules and the potential impact of this on ECP documentation. This noted that the status of an ECP dealer as a "manufacturer" or "distributor" for PG purposes will depend on the particular facts, but an ECP dealer might conclude that its role does not extend to "manufacturing" where its activities are limited to offering and selling ECP to investors on the basis of an ECP issuer's indication of the terms on which it is willing to issue ECP or an investor's indication of the terms on which it is willing to buy ECP. The note also provided further information how this assessment might impact upon ECP documentation.

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Secondary Markets

by Andy Hill, Elizabeth Callaghan and Gabriel Callsen

MiFID II/R implementation in secondary markets

Following an intense period of preparation for market participants, MiFID II and MiFIR entered into force on 3 January 2018. Overall, the "go-live" of MiFID II/R appears to have been smoother than anticipated, without causing major market disruption.

In the first quarter of 2018, ICMA has held further regional roundtables in Copenhagen, London and Vienna, focused on MiFID II/R "post-implementation". Similar to previous workshops, the roundtables targeted trading and research-related market participants from the buy side and sell side who have been heavily involved in preparations for MiFID II/R. The objective was to share experiences, assess the initial impact on trading workflow and market structure, and identify remaining challenges post-MiFID.

From the roundtables and bilateral discussions with market participants it became apparent that a number of challenges remain, some of which were expected, whilst others only emerged after 3 January 2018.

Trading workflow

With respect to trading activity, participants in ICMA roundtables reported mixed experiences. Some commented that traded volumes in fixed income had been subdued, in the first weeks of January, before recovering to pre-MiFID II levels. This short-term decrease was largely considered to be a seasonal effect rather than a direct consequence of MiFID II/R. In contrast, other market participants, notably small and mid-sized firms observed a marked and prolonged decline in trading, stemming from remaining uncertainty and a lack of official guidance from their NCAs. It was also stated that some firms had stopped providing liquidity for certain derivative products.

In a similar vein, market participants reported that trading on regulated venues[1] had increased. Some small and mid-sized participants said they executed all transactions on platforms since 3 January, having previously transacted mainly OTC. A general shift from OTC trading towards venues was somewhat anticipated, in particular for relatively liquid instruments. However, it was pointed out that trading illiquid instruments remained predominantly OTC. Overall, most participants concurred that the market share of electronic trading had risen.

The shift towards venue-trading appears to be further reflected in the increase of "move-to-venue" trades, sometimes also referred to as "processed" or "negotiated" trades. This means that trades are negotiated bilaterally and then "consummated" or formalised on a trading venue via an RFQ-to-1 between the counterparties. Participants stated that the market was adjusting to the process of "move-to-venue" trades, which may vary between trading venues and their respective rulebooks.

Market structure

A concern that had been raised prior to the "go-live" of MiFID II/R relates to identifying Systematic Internalisers (SIs). According to trade reporting requirements, it is incumbent on SIs who transact with a non-SI to publish details of the transaction via an Approved Publication Arrangement (APA). It is therefore vital for market participants to understand which counterparties are SIs for which bonds. However, ESMA's SI register does not distinguish SIs on an ISIN-level, but rather by broad categories such as "bonds", "derivatives" or "shares". As a result, in the absence of a sufficiently detailed SI register, market participants identify SIs mostly on the basis of existing relationships.

1. ie regulated markets (such as stock-exchanges), multilateral trading facilities (MTFs) or the newly created category of organized trading facilities (OTFs; such as inter-dealer brokers).

Data

A further source of concern, which relates to data, only came to light after 3 January 2018. Increasing transparency in bond (and other non-equity) markets is one of the key objectives of MiFID II/R. Under trade reporting rules, operators of trading venues and SIs are required to make quotes and details of executed transactions publicly available, free of charge after 15 minutes, in a machine-readable format. The publication is subject to pre-trade waivers and post-trade deferrals. However, in the absence of common standards, the format in which data is published by APAs and SIs varies significantly. Further feedback from members is that there is less usable data available today than before MiFID II in many instances. The data is also not "publicly available" (which is not in the spirit of MiFID II). Often an instrument ID or transaction number is needed to access the data. If the data is accessed, it may only be for a short period of time. Finally, this public data is supposed to be downloadable (in machine-readable format). Again, in many instances this is not the case. As a result, it is challenging to source, aggregate and make use of the transparency data. This is compounded by the absence of a consolidated tape provider, or "golden source", of trading activity at EU level. As requested by member firms, ICMA will further explore the development of *minimum* common data standards, in collaboration with relevant stakeholders.

With respect to transparency requirements, market participants reported furthermore that there were significant discrepancies between the number of bonds deemed liquid and illiquid bonds for trade reporting purposes. ESMA published transparency calculations of bonds in December 2017 and January 2018, setting out which individual bonds are deemed liquid or illiquid. These assessments excluded new bond issuances post 3 January 2018. However, it appeared that some platform operators considered more instruments to be liquid than those published by ESMA (again, excluding new issues).

A common theme that was raised by market participants across the EU/EEA is the lack of harmonisation when it comes to the interpretation of certain MiFID II provisions. As a Directive, MiFID II sets out common objectives whilst granting EU Member States leeway in how to achieve these, taking into account national specificities. However, the undesired side effect, in particular on cross-border transactions within the EU, is that NCAs have diverging interpretations, leading to uncertainty. For example, participants reported that NCAs have different views on what constitutes research or a "minor non-monetary benefit" (MNMB); the scope of the definition of "investment firm" in relation to buy-side firms (significantly reducing transparency and research obligations under MiFID II); or how to determine whether derivatives are TOTV (traded on a trading venue) and therefore have transparency requirements.

Conclusion

Whilst it is too early to assess the wider impact of MiFID II/R, ICMA will hold further regional "post-implementation" Q&A roundtables across Europe. ICMA will continue to address issues raised in the Q&A roundtables in its relevant committees, councils and working groups as well as explore industry-led solutions.

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ESMA guidance on MiFID II/R

In the first quarter of 2018, the European Securities and Markets Authority (ESMA) issued further guidance in relation to MiFID II/R to address specific issues following 3 January 2018. The following briefing is designed to provide a non-exhaustive summary of selected guidance impacting market structure and fixed income trading, notably (i) Systematic internalisers (SIs) and riskless back-to-back transactions; (ii) ESMA's opinion regarding packages and the derivatives trading obligation under MiFIR; (iii) pre-arranged/negotiated transactions for non-equity instruments; (iv) ESMA's update regarding liquidity assessments of individual bonds for trade reporting; and (v) further ESMA Q&A updates in relation to research, post-sale reporting, information on costs and charges, and inducements, released on 23 March 2018.

MiFID II/R

Overview of selected ESMA guidance in the first quarter of 2018:

28 March: Q&As on transparency topics

28 March: Q&As on market structure topics

26 March: Lists of trading venues and CCPs benefiting from a transitional exemption from the access provisions

- Under MiFIR Article 36(5)
- Under MiFIR Article 54(2)

23 March: Q&As on investor protection topics

21 March: Opinion in relation to packages and the derivatives trading obligation

7 February: Q&As on transparency topics

19 January: Updated liquidity assessments for individual bonds by ISIN

(i) Systematic Internalisers (SIs) and riskless back-to-back transactions

On 28 March 2018, ESMA issued an additional clarification in regards to SIs, matched principal trading, and other types of riskless back-to-back transactions. ESMA originally published on 5 April 2017 [Section 5, Question 22] its interpretation of "arrangements operated by an SI [which] would be functionally similar to a trading venue", and hence are not permissible.

Amongst other criteria, this would be the case where "arrangements would extend beyond a bilateral interaction between the SI and a client, with a view to ensuring that the SI *de facto* does not undertake risk-facing transactions." ESMA further stated on 28 March the following: "The concept of *de facto* riskless back-to-back transactions is not confined to pairs of transactions in the same financial instrument. Other arrangements, for example where one leg is a securities transaction and the other is a derivative which references that security, could also be deemed as having the objective or consequence of carrying out *de facto* riskless back-to-back transactions."

However, ESMA's conclusion outlined in Question 22, Section 5, remains unchanged: "ESMA highlights that the above does not prevent SIs from hedging the positions arising from the execution of client orders as long as it does not lead to the SI *de facto* executing non risk-facing transactions and bringing together multiple third party buying and selling interests. ESMA is of the view that an SI would not be bringing together multiple third party buying and selling interests as foreseen in Recital 19 [of the Commission Delegated Regulation (EU) 2017/565] where hedging transactions would be executed on a trading venue."

(ii) ESMA opinion regarding packages and the derivatives trading obligation under MiFIR

On 21 March 2018, ESMA released an opinion providing further guidance on the treatment of packages under the MiFIR trading obligation for derivatives (DTO) introduced on 3 January 2018.

ESMA stated that "only components of a package are subject to the TO [trading obligation, as specified in Commission Delegated Regulation 2017/2417] but not the package as such (ie the other components of the package)."

In the opinion, ESMA proposed a "tailored approach ensuring that, only where it is feasible to trade components of a package that are subject to the TO on a trading venue without creating undue operational or execution risk, those components need to be concluded on a trading venue. This approach applies to the following categories of packages:

- All components of the package are subject to the TO;
- At least one component is subject to the TO and all other components are subject to the clearing obligation for derivatives (CO);
- At least one component is an IRS subject to the TO and all other components are government bonds denominated in the same currency ('spread overs')."

The opinion is subject to review by ESMA in the future.

MiFIR – Article 2(1)

Definitions

(49) "package order" means an order priced as a single unit:

(a) for the purpose of executing an exchange for physical; or

(b) in two or more financial instruments for the purpose of executing a package transaction;

(50) "package transaction" means:

(a) an exchange for physical; or

(b) a transaction involving the execution of two or more component transactions in financial instruments and which fulfils all of the following criteria:

(i) the transaction is executed between two or more counterparties;

(ii) each component of the transaction bears meaningful economic or financial risk related to all the other components;

(iii) the execution of each component is simultaneous and contingent upon the execution of all the other components.

(iii) Pre-arranged/negotiated transactions for non-equity instruments

On 7 February 2018, ESMA issued further guidance with respect to "pre-arranged" or "negotiated" transactions in non-equity instruments. This type of transaction is initiated bilaterally, and formalised subsequently on a trading venue. While MiFIR explicitly sets out provisions for "negotiated" transactions in equity instruments, there is no equivalent provision for fixed income instruments.

With respect to non-equity instruments, ESMA therefore clarified that "it is possible to formalise negotiated or pre-arranged transactions on a trading venue subject to meeting the conditions for the respective waivers from pre-trade transparency set out in Article 9(1) of MiFIR [Waivers for

non-equity instruments]." A distinction is made between instruments that are not subject to the derivatives trading obligation (DTO) and those that are subject to the DTO.

With respect to "non-equity instruments that are not subject to the trading obligation for derivatives pre-arranged transactions are possible under:

(a) the LIS-waiver (first part of the sentence in Article 9(1)(a) of MiFIR),

(b) the waiver for instruments that do not have a liquid market (Article 9(1)(c) of MiFIR),

(c) the EFP [exchange for physical] waiver (Article 9(1)(d) of MiFIR) and

(d) the package order waiver (Article 9(1)(e) of MIFIR).

However, pre-arranged transactions may not be executed using the order management facility waiver (second part of Article 9(1)(a) of MiFIR) or the size-specific-to-the-instrument (SSTI)-waiver (Article 9(1)(b) of MiFIR).

Concerning derivatives subject to the trading obligation, pre-arranged transactions are only possible under: (a) the LIS-waiver (Article 9(1)(a) of MiFIR) and (b) the package order waiver (Article 9(1)(e) of MiFIR)." ESMA further stated that trading venues are responsible for ensuring that "pre-arranged" transactions comply with relevant regulations.

In addition, ESMA issued guidance with regard to orders held in an order management facility of a trading venue. Further information can be found here [Question 12 in section 5 of ESMA's Q&A document].

(iv) ESMA update regarding liquidity assessments of individual bonds for trade reporting

On 19 January 2018, ESMA issued an update of the liquidity assessments for bonds in relation to MiFID II/R transparency requirements. Previous calculations were published on 6 and 22 December 2017 respectively. According to ESMA, the update included "bond instruments (except ETCs and ETNs), traded for the first time on a trading venue between 1 November 2017 and 2 January 2018 (included)."

As a result, a total of 803 bonds were deemed liquid (+242 compared to the previous TTCs released on 22 December 2017). With respect to corporate bonds, the number of liquid instruments increased by 117 and totals 270. The list of individual ISINs is available on ESMA's website. This excludes new issues.

As a reminder, the transitional transparency calculations (TTC) for the liquidity assessments of bonds are applicable until 15 May 2018 and may be revised, if deemed necessary, by ESMA. It is stated that "the next version of the liquidity assessment for bonds will be published on 1 May 2018", applicable from 16 May 2018 to 15 August 2018. Subsequently, the liquidity assessments will be revised on a quarterly basis.

Latest updates of the FAQ document issued by ESMA are available on its website.

(v) Further ESMA Q&A updates released on 23 March 2018

On 23 March 2018, ESMA issued further Q&A updates in relation to MiFID II/R investor protection topics. With respect to research in the context of inducements, ESMA provided the following clarifications:

- *Macroeconomic analysis:* ESMA considers that "openly available" in the context of written material should mean that there are no conditions or barriers to accessing it, for example a necessary log-in or sign-up, or the submission of user information by a firm or a member of the public, in order to access material;
- *FICC research:* ESMA specifies that where FICC material is made openly available to all investment firms or the general public, it should be made so on the same basis as in Question 8 [macroeconomic analysis], ie there are no conditions or barriers to accessing it.

Other questions and answers include post-sale reporting in relation to retail client accounts; information on costs and charges, and the use of product costs as presented in the PRIIPs KID by investment firms; inducements and the provision of portfolio management services; and clarifications with respect to the term "ongoing relationship" within MiFID II/R and related legal texts.

Further information on the ESMA guidance mentioned above can be found on ICMA's MiFID II secondary markets website.

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MiFID II/R in Asia-Pacific

In March 2018, ICMA held two briefing sessions on MiFID II/R for its Asia-Pacific members, in Singapore and Hong Kong. This was an opportunity to share with regional members some of the key post-implementation issues that had been raised in the recent European roundtables, as well as a chance to hear what the key concerns and challenges are from the perspective of ICMA's Asia-Pacific members.

What becomes clear is that there is a significant amount of interest in the roll-out and implications of MiFID II/R among local firms, and while the subsidiaries and branches of larger, more global institutions seem to be have been well prepared going into implementation, there remains a fair degree of confusion among more regionally focused firms. In particular, there seems to be a need to understand better the extraterritorial effects of MiFID II/R, especially the extent to which it directly or indirectly applies to non-EU firms, and how this affects operating and business models. Most importantly, the requirement seems to be for credible, simplified, and pragmatic information. A number of firms noted that much of the information they receive either comes from their global counterparties or from the vendor community offering "MiFID solutions", with a tendency for this to be quite broad and technical in nature, often leading them to question its relevance.

Key areas of concern raised include the re-writing of terms of business by EU and global counterparts, the implications of distributing research into the EU, data requests by EU trading venues and counterparties to support transaction reporting, the expectations of EU clients around best execution, and product governance requirements for Asian entities distributing new issues in Europe. Asian institutions also sought more clarity on ESMA's latest guidance regarding Legal Entity Identifiers and potential implications of non-compliance.

On the other hand, the direct market impact of MiFID II/R in the Asia-Pacific region seems to be less than originally feared so far. Apart from some operational and documentation inefficiencies immediately following the implementation date at the start of the year, EU and Asian firms have reported little to no change in liquidity, trading venues, or trading dynamics attributable to MiFID II/R requirements or restrictions. ESMA's list of in-scope bonds for MIFID II purposes has also provided some comfort to the regional markets, as only 14 liquid bonds from nine major issuers are included for Asia-Pacific (excluding Australia, New Zealand, and Japan).

Local firms are also interested to monitor the impacts, successes and failures of MiFID II/R from a European perspective, as regional regulators are also closely following its roll-out to learn the lessons from the European experience to help inform and calibrate their own regulatory initiatives. In particular, regulatory transaction reporting, post-trade transparency and best execution requirements seem to be on the agenda of a number of regional authorities.

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Review of the ICMA Secondary Market Rules & Recommendations

ICMA's Rules and Recommendations for the Secondary Market apply to transactions in international securities – an international security is defined as a security intended to be traded on an international, cross-border basis (ie between parties in different countries) and capable of settlement through an international central securities depository or equivalent. All transactions between members of ICMA involving international securities (as defined within the rules) are subject to ICMA's Rules and Recommendations, unless specifically agreed otherwise by the parties at the time of concluding a transaction.[2]

ICMA, through its Secondary Market Practices Committee (SMPC), seeks continuously to review and, where appropriate, update the Secondary Market Rules and Recommendations (SMR&Rs) to ensure relevance and consistency with market best practice and market regulation. In light of evolving debt capital market structure and practice, as well as the ongoing implementation of regulation, ICMA intends to consult with members on a number of aspects of its SMR&Rs throughout 2018.

Rule 407

Between 22 February and 23 March 2018, the SMPC consulted members on the appropriateness and wording of Rule 407 ("Claim against the seller"), which relates to negative interest rate claims against defaulting sellers in the event of settlement fails. ICMA will publish the results of the consultation in the coming weeks, but the responses suggest that, for the most part, members are generally happy with the Rule.

Special situations

On 3 March 2018, the SMPC asked members to provide their thoughts and possible recommendations with respect to "Special Situations". In particular, the event of a corporate action, restructuring, or bail-in that occurs after a trade is executed, but before settlement of the securities.

Members are provided with the following non-exhaustive scenarios for their consideration:

(i) Issuer default or bail-in post trade date, but before intended settlement date.

(ii) Issuer default or bail-in post intended settlement date.

(iii) Corporate action post intended settlement date.

The topic is scheduled for discussion at the next meeting of the SMPC on 3 May 2018, and members with a view on this are encouraged to liaise with their firm's SMPC representative, or to reach out directly to the SMPC Secretariat.

Buy-ins and sell-outs

In April 2017, ICMA updated its buy-in and sell-out rules with a view to improving their efficiency and practicability, particularly in light of more challenging market conditions. Following a lengthy consultation process with member firms, the ICMA Executive Committee, in close consultation and agreement with the SMPC, unanimously resolved to amend the Buy-in and Sell-out Procedures. Most significantly, the revised rules remove the requirement to appoint a buy-in (or sell-out) agent and provide for the party initiating a buy-in/sell-out to execute the procedure themselves (subject to certain limitations). The new rules also allow for greater flexibility for the initiating party in determining the timing of the execution of the buy-in/sell-out.

Ongoing feedback from both buy-side and sell-side participants suggests that the changes have made the buy-in process far more efficient and have helped firms to manage their settlement risk more effectively.

However, it is largely anticipated that the technical standards for the mandatory buy-in regime outlined in CSD Regulation will finally be passed into European law in the coming months (see article in this section), which will radically change the nature of the buy-in mechanism for many EU investment firms, as well as their non-EU counterparties. While the eventual Regulation is not expected to come into force until the second half of 2020, ICMA will respond by undertaking extensive work with its members to revise the ICMA buy-in rules, not only to ensure compliance and compatibility with the regulatory requirements, but also to provide *standardised market best practice* to help address many of the inefficiencies in the Regulation, as well as to mitigate some of its more disruptive impacts.

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2. Unless otherwise stated, the Rules and Recommendations do not apply to the syndication and allotment process or to repurchase and to other transactions entered into under the GMRA or similar master agreements.

CSDR mandatory buy-ins: secondary markets

In February 2016, ESMA published the draft regulatory technical standards (RTS) for the mandatory buy-in process provided for in the CSD Regulation (CSDR) – a provision which continues to be strongly criticised by the industry. While ICMA and the industry appreciated ESMA's attempts to re-draft the RTS to address a number of the more problematic elements in the Level 1 Regulation, many of the key issues inevitably remain, not least the mandatory nature of the process (including forced cash compensation where the buy-in is unsuccessful), an asymmetry in the settlement of the buy-in or cash compensation differential (the so-called "CSDR put"), and a lack of flexibility in the timing of the buy-in process.

The widely understood unintended consequences of the CSDR mandatory buy-in regime include:

- a significant increase in risk for market makers providing offer-side liquidity;
- an increase in market risk for investors who may be forced out of their long positions in return for unpredictable (and unmanageable) cash compensation;
- a powerful disincentive to lending securities, given the lack of contractual interoperability between mandatory buy-ins and repo/lending agreements;
- a break-down in the market's ability to maintain fair value between cash instruments and derivatives;
- the heightened likelihood of multiple buy-ins being triggered by single fails; and
- increased market volatility and instability.

Research undertaken by ICMA in cooperation with its market-making members highlights that offer-side pricing and liquidity for bonds will be significantly negatively impacted following the implementation of mandatory buy-ins, and that the overall market risk and costs being borne by buy-side firms and their underlying investors will markedly increase.[3] The corporate and emerging market bond markets will be most severely impacted, which will be detrimental to issuers, as well as investors.

ICMA has long advocated that the mandatory buy-in regime should only be enforced as a last resort, and that regulators and market participants should continue to pursue more appropriate and less destabilising initiatives to improve and maintain bond market settlement efficiency.[4]

Despite the draft RTS having been kept on hold for more than two years, it is now expected that the European Commission will accept the RTS in the coming months, with the likelihood that they will be approved by the co-legislators before or soon after the summer recess. Given a recommended two-year delay for implementation in the RTS, the mandatory buy-in regime is thus thought likely to now come into application in the second half of 2020.

Once the RTS are finalised, ICMA will look to work with its members to:

(i) review and revise the ICMA buy-in rules to ensure that they not only support compliance and consistency with the regulatory requirements, but that they also continue to provide standardised market best practice for fixed income buy-ins and sell-outs;

(ii) review the GMRA in light of the fact that some securities financing transactions (SFTs) will be in scope of the regulation, as well as looking at the contractual basis risk that will exist between mandatory buy-ins and GMRA mini close-outs.

Meanwhile, ICMA, led by its Secondary Market Practices Committee (SMPC), and in coordination with the broader market, will continue to advocate for the regulation to be appropriately revised before it comes into force.

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3. See ICMA, 2015, CSDR Mandatory Buy-in Impact Study

4. See ICMA Position Paper on CSDR Settlement Discipline, May 2017

ICE Data Services Corporate Bond Market Liquidity Tracker

March 2018

Liquidity Tracker

Source: ICE Data Services

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.

Commentary

The trackers are of particular interest going into 2018 in light of the implementation of MiFID II/R and the potential implications for EUR and GBP corporate bond market liquidity. While there is the usual seasonal decline in liquidity across all markets going into year-end, EUR and GBP IG and HY liquidity seems to recover quite quickly, reverting to pre-year-end levels, which corroborates the anecdotal evidence (see earlier article on MiFID II implementation). Perhaps more notable is the sharp drop in liquidity in USD IG and HY in early February, which seems to be closely correlated with the sell-off in US credit spreads. A steady decline in GBP HY liquidity can also be observed over Q4 of 2017, which appears to have stabilized since the beginning of 2018.

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The "stickiness" of euro credit spreads

ICMA's secondary markets team keeps a close watch not only on credit market liquidity, but also on credit spreads, particularly as these are driven by market dynamics such as central bank purchase programmes. For instance, ICMA updates on its website the monthly cumulative ECB purchases under its Corporate Sector Purchase Programme (CSPP), overlaid with the iTraxx Main EUR 5-year index, as well as more general credit market data, including cash bond and CDS indices, relative secondary market activity, and corporate bond ETF inflows and outflows.

Therefore, the team was particularly interested to monitor how European credit spreads behaved in response to the reversal in sovereign bond yields that began in mid-December, and the sell-off in European stock markets that began in late January.

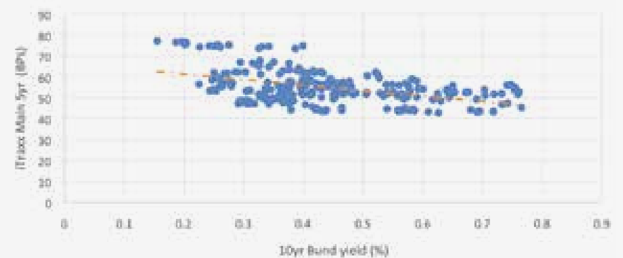
Plotting the iTraxx main (5-year) index against German 10-year yields, shows that IG credit spreads remained relatively range-bound despite the reversal in underlying bond yields. In the period that German 10-year yields rose from 0.30% to 0.76%, the iTraxx only widened from 48.2bp to 52.9bp (peaking at 56.4bp). It is only in the last week of March that credit spreads have seen sustained widening, with the iTraxx spiking above 60bp for the first time in almost a year, while Bund yields, which peaked in mid-February, continue to grind lower.

Germany 10yr Yield vs iTraxx

Source: ICMA analysis, based on Bloomberg and Markit data

A scatter plot of 10-year Bund yields and the iTraxx help to highlight the stickiness of credit spreads as bond yields moved higher, with most observations clustered in a 40bp to 60bp range, despite a wide range in Bund yields.

iTraxx Main vs Germany 10yr Yield



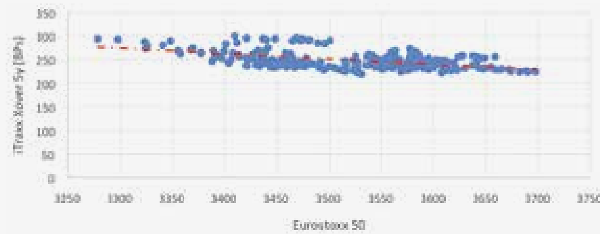
Source: ICMA analysis, based on Bloomberg and Markit data

The recent widening in credit spreads seems to be more closely correlated with moves in the equity markets (in turn driven by macroeconomic news – namely the fear of a global trade war). But again, this relationship, until very recently, has also proven to be quite sticky. The below charts plot the iTraxx X-over (5-year) index against the Eurostoxx 50 index. The charts show that over the past 12 months the iTraxx X-over has remained largely in a 220-250bp range, and even as the Eurostoxx 50 sold-off from a high of 3672 to a low of 3325 from late-January to early-February (a fall of -9.4%), the X-over index only widened 50bp. It is only in the last week of March that we see the X-over push above 290.

Eurostoxx 50 vs iTraxx Xover

Source: ICMA analysis, based on Bloomberg and Markit data

iTraxx Xover vs Eurostoxx 50

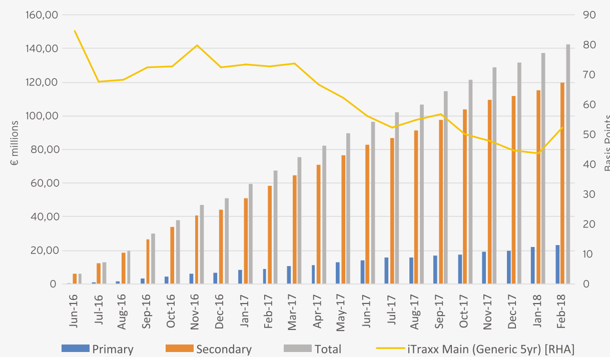


Source: ICMA analysis, based on Bloomberg and Markit data

Whilst one would ordinarily expect a greater sensitivity in credit spreads to both underlying yields and equity market movements, it would seem as if spreads have largely been desensitised as a result of the CSPP (see below chart). However, the recent weeks suggest that spread volatility may be returning – something that is only likely to be accentuated by the prospect of ECB tapering in the coming months.

Spread volatility may be returning – something that is only likely to be accentuated by the prospect of ECB tapering in the coming months.

CSPP Cumulative Purchases and iTraxx Main



Source: ICMA analysis, based on ECB and Bloomberg/Markit data

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Repo and Collateral Markets

by David Hiscock and Alexander Westphal

SFTR implementation

The final technical standards specifying the details of the extensive reporting regime for repos and other securities financing transactions (SFTs) to be introduced by the EU SFT Regulation (SFTR) are still being reviewed by the European Commission. Following some delay in the process, approval of the standards by the Commission is now expected to happen in April or May this year. Subsequently both Council and European Parliament will have another opportunity to review the proposals. Only once these are formally adopted and published a 12-month transition period will start ahead of the actual reporting "go-live" for banks. Overall, we currently expect that the reporting will probably begin in Q3 2019 for banks and investment firms and a few months later for other market participants. This gives the industry a bit more than a year to prepare implementation, which is not a lot of time considering the scale of the challenge. Given the extent of the information required, the SFTR is expected to change the way repos and other SFTs are traded and processed today.

The ICMA European Repo and Collateral Council (ERCC) is driving the industry's implementation work in relation to repo through its SFTR Task Force. The SFTR Task Force is a cross-industry group, covering users, trade repositories and other service providers. The rapidly increasing number of members since the start of this year clearly indicates a growing awareness in the industry of the task ahead and a shift of resources away from MiFID II/R towards SFTR.

In terms of priorities for the group, the key focus at this stage remains on the bilateral SFTR reconciliation exercise for repo and buy/sell-back trades launched by the ERCC SFTR Task Force in June 2017. While progress in relation to this initiative has been initially rather slow, the project has more recently gained significant momentum, also thanks to the vendors represented in the group who have started to be involved. Solutions provided by vendors have reduced significantly the burden for users to participate and have therefore helped to get more firms on board. Feedback from the reconciliation exercise is expected over the next few weeks and will help to inform the work of the Task Force going forward by highlighting the key pain points in relation to SFTR which need to be tackled through common definitions and market practices.

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CSDR mandatory buy-ins: repo markets

It is widely anticipated that the draft regulatory technical standards (RTS) for the CSDR mandatory buy-in regime, submitted by ESMA in February 2016, will receive European Commission approval in the second quarter of 2018, and, soon after, be passed into law by the co-legislators. The final RTS are expected to remain broadly similar to the draft RTS, and the likely impacts of this for bond market functioning and stability are discussed in the Secondary Markets section of this ICMA Quarterly Report.

The CSDR mandatory buy-in regime is expected to come into application 24 months after being passed into law, which currently points to the second half of 2020.

Whilst securities financing transactions (SFTs) with a

maturity of less than 30 calendar days are expected to be exempt from the mandatory buy-in rules, this nonetheless will have significant implications for the repo and securities lending markets.

First, to the extent that SFTs are in scope of mandatory buy-ins, this will require a review of the GMRA (and GMSLA) with respect to the application of the mini close-out provisions.

Second, from a central clearing perspective, it will no longer be possible to net in-scope and out-of-scope SFTs, requiring separate netting pools, so reducing netting efficiency and increasing clearing costs for members.

Finally, the CSDR fails to address the inherent link between cash bond and SFT markets. A deep, liquid SFT market is reliant on holders of securities to lend their holdings back into the market. However, lending securities runs the risk of not having them returned in time to settle any subsequent sales. In the event of a failing SFT end-leg causing a cash trade to fail, there is a risk of a buy-in being issued against the failing cash sale. While the failing end-leg of the SFT could in turn be subject to a mini close-out, this is not the same as a buy-in, either in terms of timing or the contractual framework, and it may not be possible to align the two from an economic or risk perspective.

Currently, this risk is viewed as relatively low and manageable by both bilateral and agency lenders. However, in a mandatory buy-in world, the "contractual basis risk" increases significantly, with the likely outcome that the economics of lending securities no longer provide an (already marginal) incentive to lend. This is particularly pertinent to less liquid securities, such as corporate bonds and emerging markets.

ICMA, led by its Secondary Market Practices Committee (SMPC) and the European Repo and Collateral Council (ERCC) Committee will look to review the implications for both the ICMA Buy-in Rules and the GMRA, while also continuing to advocate for the regulation to be appropriately revised before it comes into force

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Other regulatory reforms

On 8 January 2018, ESMA published a public consultation (for comment by 28 February) on draft guidelines, which aim to clarify the implementation of anti-procyclicality provisions for CCPs under EMIR. EMIR requires CCPs to monitor and account for procyclical effects of margins and make disclosures on its risk management practices including the models they use for the calculation of margins; and CCPs also need to implement anti-procyclicality margin measures.

These draft guidelines are addressed to national competent authorities that supervise CCPs authorised under EMIR. They seek to promote consistent and uniform application of EMIR and its RTS on: (i) the monitoring of margin procyclicality; (ii) the implementation of anti-procyclicality margin measures; and (iii) the disclosures to facilitate margin predictability. The draft guidelines address the observations made in the *EMIR Review Report No. 2* on the efficiency of margin requirements to limit procyclicality and the *2016 Peer Review on the Supervisory Activities on CCP's Margin and Collateral Requirements*. Considering feedback, ESMA will finalise the guidelines within the first half of 2018.

The ICMA ERCC's duly submitted response flags the importance of European repo and collateral markets in the context of CCP clearing; and highlights that great care should be taken to fully assess the way in which such anti-procyclicality measures are calibrated.

On 24 January, the European Commission opened a consultation (for comment by 21 February) regarding a new draft Delegated Regulation, amending an existing Commission Delegated Regulation, with regard to the liquidity coverage ratio (LCR). Of note from the ICMA ERCC's perspective, the second paragraph of section 1.2 of the consultation paper states that:

"The most important amendment is that the calculation of the expected liquidity outflows and inflows on repos, reverse repos and collateral swaps transactions should be fully aligned with the international liquidity standard developed by the BCBS. Although the treatment of those transactions in the LCR Delegated Regulation followed that in the CRR and had not been challenged during the many discussions preceding the adoption of the LCR Delegated Regulation, the request is that the cash outflows calculation should be directly linked to the prolongation rate of the transaction (aligned with the haircut on the collateral provided applied to the cash liability, as in the BCBS standard) rather than to the liquidity value of the underlying collateral. This approach should also be followed for collateral swaps. Generally, for repos, reverse repos and collateral swaps the language should be more closely aligned with the BCBS standard. This change will ensure that outflows and inflows on the same transactions are symmetrical and will thereby facilitate efficient liquidity management, particularly by internationally active banks."

Related to this, at the start of the second paragraph in the impact assessment section, at 1.3 in the consultation paper, it states that "The impact of the change to outflows and inflows on repos, reverse repos and collateral swaps transactions should be relatively neutral or negligible since

the substantive change is very minimal."

Among the other changes proposed in this new draft, it is also interesting to note the third paragraph of section 1.2 of the consultation paper, which starts: "The second substantive amendment concerns the treatment of certain reserves with central banks and non-EU Public Sector Entities (PSEs) that are not rated at least ECAI 1." Finally of note, according to draft Article 2 on the last page of the consultation, it is envisioned that the new rules, once finalised, will only apply "from 18 months after the date of" their formal publication in the EU's *Official Journal*.

On 27 February, the BCBS issued for consultation, *Pillar 3 Disclosure Requirements: Updated Framework*, requesting comments by 25 May. Pillar 3 of the Basel framework seeks to promote market discipline through regulatory disclosure requirements. Many of the now proposed disclosure requirements are related to the, December 2017, finalisation of the Basel III post-crisis regulatory reforms.

In addition, this BCBS publication proposes new disclosure requirements on asset encumbrance, which are described on pages 7-8 of the consultative paper (11-12 of the pdf) and in Template ENC, on pages 56-57 (60-61 of the pdf). For these purposes, encumbered assets are defined as "assets which the bank is restricted or prevented from liquidating, selling, transferring or assigning due to legal, regulatory, contractual or other limitations." It is also clearly stated that transactions conducted by banks which could possibly give rise to encumbered assets include:

- secured financing transactions, including repurchase contracts and arrangements, securities lending, collateral swaps and other forms of secured lending;
- collateral agreements, eg collateral placed for the market value of derivative transactions; and
- collateral placed with clearing systems, central counterparties and other infrastructure institutions as a condition for access to service (including default funds and initial margins).

On 16 March, the European Commission launched a short, exploratory consultation, on the finalisation of Basel III. This seeks input on the various elements of the agreed, 7 December 2017, package of reforms to finalise the Basel III framework (which were described in this section of Issue no 48 of the ICMA Quarterly Report). These comprise six key elements, including minimum haircut floors for non-CCP cleared SFTs, to limit procyclicality of these transactions and the build-up of excessive leverage in the financial system.

With respect to this, the most obviously significant paragraphs in the consultation paper are 1.10 and 1.11, to which the ICMA ERCC is responding (by the 12 April deadline). These read as follows:

The formula for repo-style transactions covered by master netting agreements has been revised to better reflect diversification benefits.

1.10. In the credit risk mitigation framework, the comprehensive approach for collateralised transactions has been simplified and at the same time been made more risk-sensitive and comparable across banks. In particular, the applicable supervisory haircuts have been recalibrated and the use of internal estimates (own-estimates of haircuts, value-at-risk model for certain securities financing transactions (SFTs)) has been removed. In addition, the formula for repo-style transactions covered by master netting agreements has been revised to better reflect diversification benefits.

1.11. Furthermore, the BCBS specified the treatment of certain non-centrally cleared SFTs with certain counterparties. The revised framework sets out minimum haircut floors and determines that in-scope SFTs which do not meet the haircut floors must be treated as unsecured loans.

Particularly regarding 1.11, one thing which the ERCC will do in its response will be to draw attention to the Commission's own final report under SFTR article 29(3), published on 19 October 2017 (which was described in this section of Issue no 48 of the ICMA Quarterly Report), which concluded that there should not be EU legislation on mandatory haircuts until there is SFTR data available to inform the correct actions to take.

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Repo and collateral-related research

On 30 January 2018, the ECB published the results of the December 2017 survey on credit terms and conditions in euro-denominated securities financing and OTC derivatives markets (SESFOD), which reported that, on balance, credit terms offered to counterparties in SFTs had remained basically unchanged over the three-month period from September to November 2017. Regarding the provision

Several jurisdictions have made substantial improvements to the wholesale repo and funding data they submitted.

of finance collateralised by euro-denominated securities, survey respondents reported that, on balance, the maximum amount of funding, the maximum maturity of funding and haircuts had all remained basically unchanged for many types of collateral. The survey also indicated that client demand had increased for most collateralised funding, in some cases owing to the impending year-end. As in the previous survey round, the liquidity and functioning of markets had remained basically unchanged for most types of underlying collateral.

On 5 March 2018, the FSB published the *Global Shadow Banking Monitoring Report 2017*, which presents the results of its seventh annual monitoring exercise to assess global trends and risks from shadow banking activities. The 2017 monitoring exercise covers data up to end-2016 from 29 jurisdictions, which together represent over 80% of global GDP, including, for the first time, Luxembourg. Also, for the first time, the report assesses the involvement of non-bank financial entities in China in credit intermediation that may pose financial stability risks from shadow banking, such as maturity/liquidity mismatches and leverage.

In light of the FSB's regulatory framework for haircuts on non-centrally cleared securities financing transactions (FSB (2015c)), the FSB data collection template was expanded, starting in the 2016 monitoring exercise, to include items from the liability side of the balance sheet, so as to capture historical data on wholesale funding and repos of the main financial sectors. The information presented in the 2016 report has been greatly improved upon, as several jurisdictions have made substantial improvements to the wholesale repo and funding data they submitted for the 2017 exercise. These improvements included providing data on wholesale funding or repos for the first time, providing a more extensive set of historical data than had been previously submitted, or providing more comprehensive data.

The 2017 monitoring report's executive summary includes that: "Other Financial Intermediaries (OFIs) have overall become less reliant on wholesale funding and repo, while banks' overall reliance on wholesale funding and repo as a source of funding has changed little since 2011. Total repo assets of banks and OFIs have increased since 2009, reaching $8.2 trillion at end-2016, and their repo liabilities reaching $7.9 trillion. OFIs continue to be net providers of cash to the financial system from repos, while banks remain net recipients of cash through repo, as reflected in net repo positions (repo assets minus repo liabilities) of these entities."

Section 2.5 of the report, at pages 30-33 (33-36 of the pdf), covers the more detailed analysis regarding wholesale funding and repos. This recognises that repos "are important funding sources for banks as well as non-bank financial entities such as broker-dealers and hedge funds, while noting that they can also be used by non-bank financial entities to create short-term, money-like liabilities, facilitating credit growth and maturity/liquidity transformation outside the regular banking system" – which can pose financial stability risks. "Wholesale funding may also increase interconnections among financial institutions and contribute to procyclicality."

In relation to enhancing system-wide monitoring and dampening procyclicality and other financial stability risks associated with SFTs, the FSB has approved in October 2017 the operational arrangements to initiate data collection and aggregation of global SFTs, beginning with end-2018 data. *Reporting Guidelines* for this data collection were published alongside this latest monitoring report.

Published on 19 March, *Leverage – A Broader View*, is an IMF staff working paper which starts from the observation that traditional measures of leverage in the financial system tend to reflect bank balance sheet data. The paper argues that these traditional, bank-centric measures should be augmented by considering pledged collateral in the financial system since pledged collateral provides a measure of an important part of nonbank funding to banks.

From a policy perspective, the paper suggests that a broader view on leverage will enhance our understanding of global systemic risk and complement the theoretical work in this field by providing a link from micro-level leverage data to macro aggregates such as credit to the economy. The papers closing conclusion is the suggestion that "international fora also request information on the extent of pledged collateral (and other off-balance sheet transactions) that are not accounted for on the balance sheet", as this "information can augment the leverage data at a national level with an additional "cross-border leverage" metric."

On 20 March, ESMA published its latest *Trends, Risks, and Vulnerabilities (TRV) Report (No 1, 2018)*, noting that European securities markets, infrastructures and investors remain at risk. Of particular note within this TRV report, on page 12 there is a two-paragraph section headed "Repo markets: growth continues", together with a chart "T.18 EA repo market volumes: Specific collateral repos drive growth" (and there are further associated charts, re market-based credit intermediation, on pages 85-86).

In addition, on page 31, there is a paragraph "Liquidity risk – high, outlook stable:" in which, among other things, it says: "Liquidity in sovereign bond markets deteriorated slightly towards the end of the year, reflected mainly in higher bid-ask spreads (R.10, R.11)" and that "The trading volume of centrally cleared repos continued to grow strongly (R.13) while collateral scarcity premia (ie the difference between general collateral and special collateral repo rates), increased again in late 2017 (R.14) reflecting possible shortages of high-quality collateral. This may increase liquidity risk and volatility in funding costs and reduce overall market confidence." (The related securities markets charts are on pages 32-34).

And, on a related note, on 19 March the ECB published a focus piece under the title *Euro Area Sovereign Bond Market Liquidity Since the Start of the PSPP*. Having acknowledged the importance of liquidity in this market, this states that, overall, "the indicators suggest that liquidity conditions in sovereign bond market have not deteriorated since the start of the PSPP (on 9 March 2015)." It remains to be seen whether such a conclusion can continue to be drawn during the period ahead.

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34th ICMA European repo market survey

The European Repo and Collateral Council (ERCC) released the results of its 34th semi-annual survey of the European repo market in March. The survey, which calculates the amount of repo business outstanding on 6 December 2017 from the returns of 64 offices of 60 financial groups, sets the baseline figure for European market size at €7,250 billion. This is the largest figure ever recorded by the survey since it began in 2001 and exceeds pre-crisis figures for the size of the repo market in Europe. After a period of four years where market size has remained static, with largely seasonal fluctuations, this survey shows growth, in terms of contracts outstanding on the survey date, of 12.3% since the last survey in June 2017 and 28.2% year on year.

Post-crisis regulation has mandated the increased use of collateral to underpin the stability of the financial system, for example in the margining of OTC derivatives. The repo market provides the mechanism by which this collateral, mostly in the form of government bonds, moves around the system. Repo market activity has however been constrained by uncertainty over the impact of post-crisis regulatory measures which have caused banks to ration their balance sheets in order to be sure of meeting regulatory ratios and the continuing effects of Quantitative Easing limiting the supply of High Quality Liquid Assets (HQLA) collateral securities, all of which culminated in major repo market dislocation at year-end 2016.

The increase in market size measured by the latest survey indicates that in 2017 at least some banks were adapting to the new regulatory environment and starting to make more balance sheet available to customers. Just under half the banks in the survey had expanded their repo books, but it remains to be seen if this growth is sustainable given the regulatory challenges that lie ahead with the implementation of the Net Stable Funding Ratio (NSFR), Central Securities Depository Regulation (CSDR), Securities Financing Transactions Regulation (SFTR) and other measures. Anecdotal evidence from the ICMA report on end-of- year conditions in the repo market in 2017 cites improvements in collateral management and a return to profitability for repo desks.

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Changing coverage of the ICMA GMRA legal opinions

By Lisa Cleary

The Global Master Repurchase Agreement (GMRA) is the most widely used contract in the international repo market. For many years ICMA has supported the use of the GMRA by obtaining legal opinions in over 60 jurisdictions on the GMRAs 1995, 2000 and more recently the GMRA 2011. The opinions cover, amongst other things, the enforceability of the agreement as a whole, and more specifically, analyse the enforceability of its netting provisions on insolvency. With the support of the ERCC Committee, ICMA will discontinue coverage of the GMRA 1995 in the GMRA legal opinions from 2019 onwards. The opinions will continue to cover the GMRA 1995 as amended by the Amendment Agreement and the GMRA 1995 as amended by the 2011 GMRA protocol (subject to certain elections being made). This measure has been considered for some time, providing the market with sufficient time to progress repapering efforts. It is important that the most up-to-date versions of the agreement are being used, reflecting the latest market practice and legal and regulatory position.

The ERCC Committee and colleagues in member firms committed considerable resources to the development of the GMRA 2011. The updated agreement reflects the default process in the post Lehman environment, changing insolvency and bankruptcy regimes, changing practice in the repo market and increased harmonisation across industry master agreements. Amongst other things, the GMRA 2011 contains important default mechanism enhancements which provide increased flexibility for the non-defaulting party and improves counterparty risk mitigation. ICMA continues to support the adoption of the GMRA 2011 through its educational and training offerings as well as the support of its legal helpdesk.

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ICMA ERCC AGM

The ERCC's 2018 Annual General Meeting (AGM) was held on 14 March, kindly hosted by BNY Mellon in the Fishmonger's Hall in London and attended by over 200 delegates.

This year's programme included presentations on the various workstreams that the ERCC is currently involved in and a panel discussion. As usual, the event was opened by ERCC Chairman Godfried De Vidts, who informed members about the outcome of the recent ERCC elections and also updated attendees on the results of the latest 34th European Repo Market Survey. This was followed by a legal update delivered by Lisa Cleary, Associate Counsel at ICMA, who informed members about the latest developments in relation to the GMRA, including the important announcement that ICMA will discontinue coverage of the 1995 GMRA in the legal opinions as of 2019 (as noted above). ICMA Senior Director Andy Hill went on to present the key findings from a recent ERCC report on the conditions in the repo market around year-end 2017. This was followed by an update on the various regulatory initiatives impacting repo markets, delivered by David Hiscock, Senior Director at ICMA. The presentation part of the event was concluded by an update from the ERCC Operations Group provided by Nicholas Hamilton, J.P. Morgan and co-chair of the Group, who covered some of the key initiatives that the ERCC is involved in on the post-trade side, including important work undertaken in collaboration with the ECB in relation to collateral management.

This led seamlessly to the concluding panel which focused on TARGET2-Securities (T2S), and the question of how to unlock the value of the new settlement environment for users, at a critical crossroads for T2S following the successful completion of the migration in September 2017. Gesa Benda, BNY Mellon, moderated the discussion with a group of market practitioners, including three ERCC Committee members, who looked at the issue both from a trading as well as from a more operational/ technical angle.

From a trading perspective, panellists commented that T2S has not had much impact in practice yet. The three main concerns in relation to settlement remain in place, namely: (i) both central bank money (CeBM) settlement in T2S and commercial bank money (CoBM) settlement with the ICSDs and agents continue to co-exist, as many clients do not have direct access to T2S, and along with this the frictions between both settlement environments; (ii) triparty repo is a very efficient way to do business but is still fragmented and requires firms to move collateral; (iii) there is still a great reliance on the ICSD Bridge which continues to create frictions. None of these aspects have improved with T2S. In addition, even more importantly, settlement costs have not decreased. Considering the substantial development costs

for T2S, it is thus in the current circumstances not easy to see the business case for the project. For the time being, T2S remains merely a technical upgrade which cannot be fully utilised yet as essential additional applications are still missing. Important aspects mentioned in this context were: (i) a solution needs to be found to allow balance sheet netting for cross-CSD settlement in T2S; (ii) a collateral management tool within T2S would be needed to allow firms to centrally manage collateral pools; (iii) T2S needs to facilitate the efficient management of intraday liquidity.

On the other hand, panellists pointed out that the degree to which firms already benefit from T2S also depends on their operational set-up pre-T2S and the manner by which they connect to the platform. Firms with a less sophisticated set-up prior to T2S will probably already reap significant benefits from the opportunities that T2S offers in terms of timely settlement messaging and additional functionalities, such as auto-collateralisation. In contrast, firms that already had a well-developed set-up pre-T2S, including an efficient European sub-custody network enabling them to better realise netting efficiencies, probably have not felt the need to make any changes to this set-up as a result of T2S and are thus not experiencing any significant improvements. Unlike regulation, T2S is also not a mandatory project for firms, so many firms have not yet reviewed their operational and account set-up. In theory, T2S should enable firms to consolidate their securities accounts into a single T2S account, similar to what has happened on the cash side with the introduction of the euro in the early 2000s. In practice however, it has become clear that such consolidation on the securities side is much more difficult to achieve than on the cash side, given the significant number of national barriers that continue to prevent a more integrated post-trade environment. Panellists stressed especially the large number of barriers that will have to be addressed by the public sector, eg in relation to withholding taxes and corporate actions, as highlighted in the recently published report by the European Post Trade Forum (EPTF).

Panellists also underlined the importance for the private sector to actively embrace the new settlement environment provided by T2S. This will require all players in the market, CSDs, custodians and market participants, to develop the necessary solutions and services, including in relation to custody and the efficient processing of corporate actions and taxes. Another important aspect will be the push for a further harmonisation of business processes. Panellists welcomed the pro-active approach taken by the Eurosystem in this context to foster further harmonisation, in particular in relation to collateral management. The planned Eurosystem Collateral Management System (ECMS), due to go live in 2022, and complementary work undertaken by the Collateral Management Harmonisation Task Force (CMH-TF) are important initiatives which are expected to benefit the market more widely and which need to be appropriately supported by the industry.

A more detailed summary of the panel discussion has been published on the ICMA website, alongside pictures from the event and all related presentations.

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For the time being, T2S remains merely a technical upgrade which cannot be fully utilised yet as essential additional applications are still missing.

Asset Management

by Patrik Karlsson and Bogdan Pop

Covered bonds

On 12 March 2018, the European Commission launched their long-awaited legislative proposal on covered bonds, in the form of a Directive on covered bonds and a Regulation amending the treatment of covered bond exposures under the CRR.

AMIC's Covered Bond Investor Council (CBIC) has followed the progress of the European Commission's deliberations with interest. On 5 January 2016, CBIC responded to the Commission's consultation on covered bonds as preparation for this legislative initiative. The CBIC did not specify a preference for harmonised rules but did not oppose them outright. On over-collateralisation CBIC agreed with a legal minimum level for all issuers but did not specify what that minimum level should be.

The Directive specifies the core elements of covered bonds and provide a common definition as a consistent and sufficiently detailed point of reference for prudential regulation purposes, applicable across financial sectors. It establishes the structural features of the instrument, a covered bond-specific public supervision; rules allowing the use of the "European Covered Bonds" label; and competent authorities' publication obligations in the field of covered bonds. The Regulation mainly deals with amending Article 129 of the CRR. The amendments add requirements on minimum overcollateralization amongst other things.

The Directive and Regulation have passed to the European Parliament and Council to undergo the ordinary legislative procedure.

CBIC has begun to prepare its position on the legislation. Subject to finalisation and agreement by members, the CBIC welcomes the initiative and the many benefits it brings to investors. In particular, CBIC welcomes the sensible principles-based approach the Commission has taken to a well-functioning asset class.

However, CBIC will also propose some targeted improvements to the text:

The CBIC welcomes the initiative and the many benefits it brings to investors.

- *eligible assets:* greater clarity on what "other high quality assets" should be;
- *third countries:* an acceleration of the third country equivalence process;
- *extendable maturities:* the addition of an issuer default trigger;
- *cover pool liquidity buffers:* (i) greater clarity on eligible liquidity buffer assets and (ii) reversing the use of LCR buffers in cover pools to allowing cover pool buffers to be used for LCR purposes

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STS securitisation

The simple, transparent, standardised (STS) Securitisation Regulation has now been published in the *Official Journal*. The STS Regulation and the CRR Amendment were published on 28 December 2017. Both texts thus entered into force on 18 January 2018, however the date of application of both the STS Regulation and CRR Amendment is 1 January 2019.

EBA and ESMA have started their work on Level 2 technical standards, by issuing five consultations this spring. The EBA

consulted on technical standards on risk retention and on technical standards on homogeneity of underlying exposures in securitisation. ESMA consulted on technical standards on content and format of the STS notification under the Securitisation Regulation, on standards on disclosure requirements, operational standards, and access conditions under the Securitisation Regulation and on technical standards on third-party firms providing STS verification services under the Securitisation Regulation.

AMIC continues to be engaged in the STS process. The greatest area of focus for investors remains the lack of progress on Solvency II reform. The Commission has still not launched its set of amendments to the Level II legislation of Solvency II to amend the capital requirements for STS securitisations. The Commission have consulted Member States. The Commission also organised a public hearing on 27 March 2018.

At the hearing, in his introductory remarks, the European Commission's Vice-President Valdis Dombrovskis noted that STS securitisation will lead to an additional €150 billion of funding to the economy. However, the technical advice issued by the European Insurance and Occupational Pensions Authority (EIOPA) on the review of the Solvency II Delegated Act is silent on any potential calibration changes. The first panel of the hearing saw a strong case put forward for re-calibrating Solvency II capital requirements for securitisation to incorporate the new STS securitisation framework and stimulate the STS securitisation market, which seems to have resonated with the European Commission's own views.

A proposal to introduce changes to the securitisation calibrations in the Solvency II Delegated Act are expected by summer 2018 in order to be introduced by January 2019 when the STS Regulation has to be applied.

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Corporate governance

The AMIC Corporate Governance Working Group has responded to the Financial Reporting Council's (FRC) consultation to revise the UK Corporate Governance Code on 28 February 2018.

The consultation focused on a number of key points, including: non-shareholder stakeholders; board members' tenure; board diversity pipeline; independence of the Chairman; minority shareholders concerns; and the remit of the remuneration committee.

In line with the remit of the Working Group, which is to look at corporate governance issues from a debt holder perspective, the AMIC response suggested that the FRC should reflect in the revised UK Corporate Governance Code the importance of debt holders among the many stakeholders and should try to encourage additional dialogue with this stakeholder group. The interests of debt holders as stakeholders are unfortunately not always considered by companies. Better engagement with debt holders could achieve better outcomes for the company and all its stakeholders.

The AMIC response also stressed the need to maintain flexibility in the revised Corporate Governance Code to allow firms to implement it in a way which best fits their business models. This flexibility can be maintained by keeping the Code mostly principles based and by continuing the current comply or explain approach.

AMIC also looks forward to contributing to the forthcoming FRC consultation on the Stewardship Code which is planned to be issued later in 2018.

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Bail-in

By Katie Kelly

The ICMA Bail-in Working Group (BIWG), a buy-side group which is a committee of, and reports into, the Asset Management and Investors Council (AMIC), recently held a seminar on bail-in and bank resolution in Frankfurt, one of a series of similar events being held in Europe.

Amid current market conditions and an expected rate rise, there remain significant difficulties in the pricing of resolution risk into capital instruments. In an ideal world, the existence of a quick, automated resolution process would make it easier for investors to gauge the probability of default and likelihood of resolution. But the reality is that resolution processes are not automatic, and the many remaining uncertainties for investors, together with a perceived high degree of discretion on the part of Single Resolution Board (SRB), only serve to compound the pricing predicament.

Obviously, fundamental balance sheet analysis is critical for pricing. Although many banks are better capitalised now than in the past, some banks' balance sheets may still lag behind in terms of remaining legacy non-performing loans (NPLs); add to this the differences in risk profiles between Additional Tier 1, Tier 2 and bail-inable senior debt, all of which in some cases has been bailed-in, but in others, has not, makes it even more difficult for investors to price capital instruments.

There are three key elements of resolution risk that will drive outcomes and, therefore, affect pricing for investors: (i) timing of the determination of failure or "likely to fail", being the difference between a liquidity shortage (but still able to qualify for emergency liquidity assistance) and actual insolvency due to illiquidity; (ii) the SRB determination as to whether a resolution is in the public interest or not, which determines whether the applicable resolution rules are under the Bank Recovery and Resolution Directive or Single Resolution Mechanism rules or national liquidation rules and (iii) which resolution tools will actually apply.

Significant progress has been made over the last 12 months with the cases of Banco Popular, Veneto Banca, Banca Popolare di Vicenza and Latvian bank ABLV testing the new resolution regime and allowing a better understanding of how authorities will interpret decisive terms. However, although these cases were an important step in gaining more transparency on the resolution process, they raise many more issues, and may be just the start of the journey. For instance, valuation reports are a fundamental tool in the overall assessment, but may still not reveal the full picture, leading to difficulties in the predictability of probability of default, likelihood of resolution and loss-given default. This is demonstrated by the litigation relating to the resolution of Banco Popular, where opacity surrounding the valuation has led to uncertainty as to whether it was fair, prudent and realistic.

The BIWG is undertaking further work in these areas, including a fresh look at pricing dynamics and rollover risk, the potential dislocation between primary market and secondary market liquidity, how the dynamic between investors and issuers affects current pricing and appetite for risk and whether investors are treating "low probability" as "risk free".

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Infrastructure finance

The FSB has released a survey on *Financing and Regulation over the Life Cycle of Infrastructure Projects* in order to gather feedback from financial institutions that are actively involved in infrastructure financing on: recent and expected trends in infrastructure finance, and on the relevant drivers of these trends; the extent to which G20 financial regulatory reforms agreed post-crisis have influenced the cost and availability of financing for infrastructure; and how significant regulations compare to other factors, such as the macroeconomic environment. A final report on financing of infrastructure investment will published by the FSB in advance of the G20 Leaders' Summit in Buenos Aires in November 2018.

There is a huge gap between a good idea and a bankable project.

Elsewhere, a global initiative comprising the ECB, OECD, Global Infrastructure Hub and Long-Term Infrastructure Investment Association is aiming to unlock infrastructure project data. Project performance data are hard to come by, especially in the developing world; much is held at the private sector level or behind paywalls, with no compulsion to disclose it. But good data are crucial for primary decision making – allocations to infrastructure portfolios, portfolio construction, investment decisions, evaluation of additionality and credit enhancement – and the data dearth is proving to be a deterrent.

There is still a lot of money looking for a home in infrastructure, and with investors improving their infrastructure capabilities in terms of funds and human resource, there is no shortage of interest. But fundamentally, projects are not being prepared fast enough, and money is not being applied to projects efficiently enough, all of which makes for a sluggish pipeline. Were this trend to continue, investors might turn their attentions elsewhere wherever opportunities arise.

A solution may lie in standardisation of disclosure and reporting requirements, documentation, administration and arbitration procedures. There is a huge gap between a good idea and a bankable project, between requirements and financing, and a lack of relevant expertise coupled with lack of project preparation and a reluctance to pay for expert advice can mean that getting an infrastructure project financed can be a long, painful and extremely document-heavy process. Standardisation could go some way to addressing these issues by ensuring that projects are understandable, comparable, simpler and more cost-effective. Some standard documents, when used and adapted appropriately and intelligently, already provide a useful starting point. Some key provisions may be capable of standardisation – such as *force majeure*, termination, material change and dispute resolution; however, once certain provisions become enshrined, they can quickly become market practice, and could bind a project in an unfavourable way.

Nonetheless, complete standardisation is very difficult to achieve – projects have to be bespoke by their nature, and with the range of differing economic situations,

jurisdictional circumstances, structural issues and myriad types of risks, it is hard to know where to start. Standardisation of levels of disclosure and reporting requirements may also prove to be a double-edged sword, exposing parties to liability if the prescribed levels are not high enough.

Meanwhile, ICMA continues to observe the activities of the Greening the Belt & Road Investor Alliance, which aims to match belt and road projects with green financing to mitigate long-term environmental effects of infrastructure. ICMA, together with AFME as part of the AFME/ICMA Infrastructure Finance Working Group, continues to explore these and other issues.

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AMIC Council in Brussels

The latest AMIC Council took place on 6 March 2018 in Brussels, hosted by BNP Paribas Fortis. The AMIC Council holds two plenary sessions annually to advise the Executive Committee of AMIC on priorities and to discuss current issues at biannual conferences. These meetings also provide excellent networking opportunities for the AMIC community.

AMIC Chairman Robert Parker gave an overview of investment sentiment indicators, including: the most crowded trades, tail risks, sector and asset allocation and overvalued markets. He also reviewed the performance in 2017 of asset classes and economic indicators, including monetary conditions, GDP forecasts, inflation trends, business and consumer confidence and economic surprises.

This was followed by a panel which focused on the intricacies of smart beta and other factor investing, elaborated how these strategies work and how they are used to complement traditional active and passive investing approaches. The panellists noted that as a third approach to investing, factor investing aspires to outperform traditional market benchmarks similar to active funds while at the same time providing the transparency and lower costs associated with passive investing.

The second panel of the day discussed sustainable finance and investor duties in the context of the recommendations issued by the High Level Expert Group on Sustainable Finance (HLEG), how this may work in practice and whether the focus of this report is too much on Environmental issues, with not enough thought given to the governance and social aspects of ESG.

The third panel discussed the shift from liquid to illiquid instruments from the perspectives of both the asset management and insurance industries, why this happened and the potential risks and consequences from prolonged exposure to this environment.

The European Commission's Vice-President for Jobs, Growth, Investment and Competitiveness, Jyrki Katainen, gave a closing keynote address to the audience. Vice-President Katainen covered recent developments in the European Fund for Strategic Investment (EFSI), Capital Markets Union (CMU) and sustainable finance.

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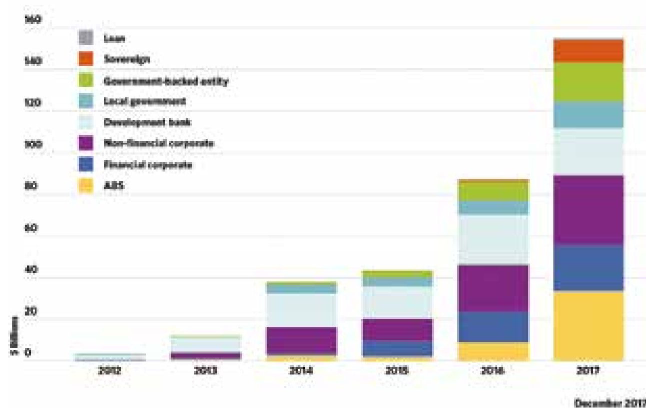
Green, Social and Sustainable Bond Markets

by Nicholas Pfaff, Valérie Guillaumin, Peter Munro and Denise Odaro

Green and social bond market developments

Growth and diversification have continued to be hallmarks of green, social and sustainable bond markets. The green bond market grew in 2017 by 78% to $156 billion (see Figure 1), with the number of new issuers accelerating (+146 vs. +c.90 in 2016), making a total of 239 issuers in 2017. The US, China, France, Germany and supranationals were the top five sources of volume. Geographic diversification continued apace, with green bond issuance reaching 37 countries, from 24 at end-2016. There was also remarkable growth of green asset-backed issuance, driven by Fannie Mae, with close to $25 billion of issuance.

Figure 1: Green Bond market issuance



Source: Climate Bonds Initiative (CBI)

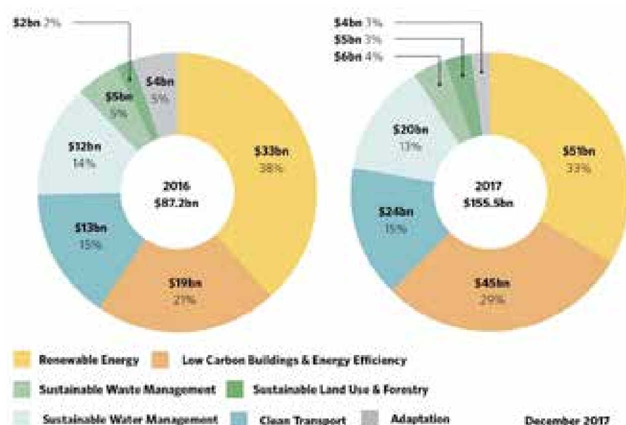
Growth and diversification continued to be hallmarks of green, social and sustainable bond markets.

Social bond issuance tripled to €8.8 billion, while sustainability bond issuance grew 54% to €26.7 billion (sources: Bloomberg, Crédit Agricole CIB, Citi, ICMA). Social and sustainability bond issuance, still at an early phase of development, remained dominated by SSA issuers, as in the early days of green bonds, although commercial banks started to become important issuers, accounting for around 13% of social and sustainability bond issuance combined.

There was more liquid green bond issuance, boosted by a trend towards sovereign issuance. Landmark issuance came from France (for total of €9.7 billion/$10.7 billion). Sovereign issuance also spread to emerging markets in 2017 – with Fiji and Nigeria taking the lead. The trend was reinforced in both developed and emerging markets in Q1 2018, with issuance at scale from Belgium (for €4.5 billion/$5.5 billion) and Indonesia – with a first green sovereign sukuk ($1.25 billion).

For green bonds the use of proceeds diversified significantly. While investments in renewable energy continue to be the most common use of proceeds, allocations to low carbon buildings and energy efficiency rose 2.4 times year-on-year (see Figure 2).

Figure 2: Green bond market use of proceeds



Source: Climate Bonds Initiative (CBI)

Among buy-side innovations was the launch by IFC of a fund for $1.5 billion, the Green Bond Cornerstone Fund, targeting green bond issuance by emerging market financial institutions and managed by Amundi. It utilises risk tranching to mitigate risk for certain portfolio investors in the fund with tighter risk budgets, as well as technical assistance to boost supply.

Key policy developments in the EU and in Asia

There were important policy developments in the EU, with key proposals including a European Union Green Bond Standard building on the GBP, as well as a Sustainability Taxonomy. These initiatives were articulated in the final report of the European Commission High Level Expert Group (HLEG) on sustainable finance and were largely taken up in a related European Commission Action Plan on sustainable finance. Both are covered in detail in the accompanying feature article in this Quarterly Report.

There were also important developments in Asia, notably in China and Hong Kong. Among these, the publication in China of a joint white paper by the Green Finance Committee of the China Society for Finance & Banking and the EIB, identifying differences between Chinese and European green classifications, with a view to working on a common language. In Hong Kong, the Government announced plans for a sovereign green bond issuance programme of up to HK$100 billion (US$ 12.7 billion), as well as plans for a grant scheme to support green bond issuance.

Industry coordination and initiatives in green finance

The Global Green Finance Council (GGFC), co-founded and coordinated by ICMA, brings together a range of leading financial trade associations. It held its latest quarterly meeting in March 2018 where the chair of the EU HLEG, Dr. Christian Thimann, gave a detailed overview of the final report of the European Commission HLEG on sustainable finance and expectations for the related European Commission Action Plan on sustainable finance. The GGFC subsequently issued a joint press release welcoming the Action Plan while also recommending prudent implementation and avoiding unintended barriers to market development.

The Loan Market Association (LMA) , together with the Asia Pacific Loan Market Association (APLMA) and with the support of ICMA, launched on 21 March 2018 the Green Loan Principles (GLP) to create a high-level framework of market standards and guidelines for use across the wholesale green loan market. The need for the initiative was originally identified in 2017 by the GGFC, of which the LMA and ICMA are both founder members, and the APLMA, which established a working group in June 2016. The GLP were developed by a working party consisting of representatives from leading financial institutions active in the green loan market, with the assistance of the Association of Corporate Treasurers (ACT) and the European Banking Federation (EBF). They illustrate how the financial industry can work together to further mainstream green finance. The GLP are described further in a separate article below.

Green Bond Principles AGM & Conference

Plans are well advanced for the 2018 GBP/SBP AGM & Conference, which are being co-hosted by The Hong Kong Monetary Authority (HKMA). The GBP and SBP AGM and Conference have become one of the most high-profile gatherings for leaders in the green, social and sustainable bond markets and increasingly for other asset classes in sustainable finance. Holding the event outside Europe for the first time constitutes recognition of the rising importance of Asian markets and policy initiatives. Further details including a registration form are available here, or by contacting the Secretariat.

Implementation of voluntary contributions to fund the GBP and SBP Secretariat

The GBP & SBP annual consultation in 2017 included a proposal to put in place a voluntary financial contribution for non-ICMA members of the Principles from 2018 to help finance the Secretariat provided by ICMA. The Secretariat has so far been funded through the general fee pool of ICMA membership although more than half of the GBP &

SBP Members and Observers are not ICMA members. An overwhelming 87% of respondents, of which a majority were not ICMA members, reacted favourably to the proposal.

After further discussion with the GBP/SBP Executive Committee, a call was held in March 2018 with GBP Members and Observers to present and discuss a proposed voluntary contribution of €10,000, to be charged on an annual basis. After positive feedback from the call, it was decided to proceed with the implementation of the proposal. The funding is now being sought from all registered Members and Observers of the Principles who are not fee-paying members of ICMA to assist in covering the costs incurred in the management, administration and development of the Principles, in addition to providing enhanced services. There are exemptions from paying this fee for NGOs and not-for-profit organisations. In place of the annual fee, Members and Observers have the option of joining ICMA as a member, which offers a wide range of additional benefits relating to regulatory, market and best practice issues among others.

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Introduction to green bonds: new ICMA training course

ICMA's new Introduction to green bonds course ran for the first time in March in London with an international audience from banks and other financial institutions, exchanges and rating agencies. Developed with the involvement of members of the GBP Excom, the new course gives a thorough and practically oriented introduction to the essentials of green bonds, introducing underlying market drivers, the evolving regulatory framework and the main features of the green bond product and market based on the GBP. The next course will run in London on 15-16 May.

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Launch of the Green Loan Principles

The Loan Market Association (LMA) has, together with the Asia Pacific Loan Market Association (APLMA), launched on 21 March 2018 the Green Loan Principles (GLP) with the support of ICMA.

The GLP aim to create a high-level framework of market standards and guidelines for use across the wholesale green loan market, whilst preserving its integrity while it develops. It also aims to ensure consistency between green loans and bonds, and especially to facilitate the refinancing by the capital markets.

The GLP indeed build on and refer to the Green Bond Principles (GBP) of ICMA. They are based on the same four core components (Use of Proceeds, Process for Project Evaluation and Selection, Management of Proceeds and Reporting) and recommendations for the use of external reviewers. They set out a clear framework to be applied by market participants on a deal-by-deal basis depending on the underlying characteristics of the transaction and are focused on the financing of eligible green projects.

The need for the initiative was originally identified in 2017 by the Global Green Finance Council (GGFC), of which the LMA and ICMA are both founder members, and the APLMA, which established a working group in June 2016. ICMA also acts as secretary to the GGFC. The GLP were developed by a working party consisting of representatives from leading financial institutions active in the green loan market, with the assistance of the Association of Corporate Treasurers and the European Banking Federation.

The publication of the GLP marks the first step towards establishing widely accepted principles in the green lending space. The objective is to significantly expand the scope of green finance internationally. It is also a great example of what can be achieved by the financial industry in the green space through the dialogue and coordination of the GGFC. Looking ahead, the working party will be seeking to expand the scope of the GLP to capture alternative models of green finance.

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International Regulatory Digest

by David Hiscock and Alexander Westphal

G20 financial regulatory reforms

The Financial Stability Institute (FSI) and the International Association of Deposit Insurers (IADI) organised their eighth joint conference on bank resolution, crisis management and deposit insurance, on 31 January-2 February 2018, at the BIS in Basel. The event was attended by close to 250 central bankers, banking supervisory officials and deposit insurers representing 130 financial authorities in 80 jurisdictions worldwide.

Alongside various panel discussions, keynote addresses were given by Mark Branson, CEO of the Swiss Financial Market Supervisory Authority and Chair of the FSB Resolution Steering Group, and Sir Paul Tucker, Chair of the Systemic Risk Council and Senior Fellow at the Center for European Studies at Harvard University; and closing comments were delivered by Agustín Carstens, BIS General Manager.

On 27 February, the BCBS issued, for consultation, *Pillar 3 Disclosure Requirements – Updated Framework* (for comment by 25 May). Many of these proposed disclosure requirements, which would complete the Pillar 3 framework, are related to the finalisation of the Basel III post-crisis regulatory reforms in December 2017 and include new or revised requirements:

- for credit risk (including provisions for prudential treatment of assets), operational risk, the leverage ratio and credit valuation adjustment (CVA);
- that would benchmark a bank's risk-weighted assets (RWA) as calculated by its internal models with RWA calculated according to the standardised approaches; and
- that provide an overview of risk management, key prudential metrics and RWA.

In addition, new disclosure requirements are proposed on asset encumbrance and capital distribution constraints.

On 28 February, the FSB and the Deutsche Bundesbank announced that they are seeking academic paper submissions (by 15 April) for a plenary session on the *Post-Implementation Evaluation of the G20 Financial Regulatory Reforms*, at the 2018 Annual Meeting of CEBRA. This conference is co-organised by the Research Center SAFE (Sustainable Architecture for Finance in Europe) and will take place at Goethe University in Frankfurt on 20-21 August.

On 12 March, the BCBS published overviews of follow-up actions taken or planned by member jurisdictions as of end-2017 to address deviations from the Basel standards that were identified as part of the BCBS's Regulatory Consistency Assessment

Programme (RCAP), covering assessments that were completed and published as of end-2016.

These follow-up reports are published on the BCBS's website alongside the original RCAP reports and are prepared by authorities in each jurisdiction that has been assessed. The reports, which have not been reviewed or evaluated by the BCBS, outline the actions a jurisdiction has already taken or has planned. A summary of follow-up actions taken or planned by member jurisdictions is also published. Follow-up reports for assessments completed and published as of end-2017 will be published in 2019.

The BCBS published an outline of discussions at its meeting on 15-16 March in Basel. The BCBS discussed its work programme and strategic priorities for 2018-19. The work programme centres on four broad themes: (i) finalising existing policy initiatives and initiating targeted policy development; (ii) ensuring full, timely and consistent implementation of the Committee's post-crisis reforms; (iii) promoting strong supervision; and (iv) evaluating and monitoring the impact of post-crisis reforms, as well as assessing emerging risks.

The BCBS discussed its current policy work and:

- agreed to consult on a set of limited and targeted revisions to the revised market risk framework published in January 2016 – BCBS members reiterated their expectation of full, timely and consistent implementation of this framework by 1 January 2022;
- following its consultation on possible revisions to the assessment framework for G-SIBs, the BCBS agreed on a revised framework, which will soon be published; and
- agreed on a set of criteria and capital treatment for short-term STC securitisations – the accompanying standard will be published in due course.

As part of its efforts to ensure full, timely and consistent implementation of its reforms, the BCBS agreed to explore ways to conduct preliminary consistency assessments of members' forthcoming draft rules to implement the Basel III standard, which was finalised in December 2017; and agreed to commence developing a methodology for how such assessments might be conducted, on the basis that such assessments would be voluntary. The BCBS also discussed its ongoing initiatives to promote strong supervision, approving a report for publication on early supervisory intervention practices.

Regarding its work on evaluating and monitoring the impact of post-crisis reforms, the BCBS took note of a recent stocktake of identified transactions and behavioural responses by banks that could potentially constitute a form of regulatory arbitrage; and agreed to further assess a set of these transactions. As part of its regular horizon scanning, the BCBS also exchanged views on recent market and supervisory developments, including the impact on the banking system of volatility in financial markets in the first quarter of 2018, and implications of the emergence of crypto-assets. The BCBS also published an updated set of FAQs on the Basel III standardised approach for measuring counterparty credit risk exposures.

On 18 March, the FSB published a letter from FSB Chair, Mark Carney, to G20 Finance Ministers and Central Bank Governors ahead of their meetings in Buenos Aires, on 19-20 March. The letter notes that the current backdrop of strong and balanced global growth is underpinned by a resilient global financial system that is the product of determined efforts by the G20 and FSB over the past decade. The letter sets out the FSB's priorities under the Argentine Presidency, which are designed to reinforce the G20's objective of

The BCBS took note of a recent stocktake of identified transactions and behavioural responses by banks that could potentially constitute a form of regulatory arbitrage.

strong, sustainable and balanced growth through:

- vigilant monitoring to identify, assess and address new and emerging risks;
- disciplined completion of the G20's outstanding financial reform priorities;
- pivoting to policy evaluation to ensure the reform programme is efficient, coherent and effective; and
- optimising how the FSB works in order to maximise its effectiveness.

Regarding the second of these, the FSB is making significant progress on the G20's outstanding financial reform priorities, with a large number of initiatives on track to be completed by or before the Buenos Aires Summit. During the course of the year the deliverables to the G20 will include, among others, leverage measures for investment funds; guidance on financial resources available to support CCP resolution; a cyber security lexicon; and the private sector-led Task Force on Climate-related Financial Disclosures' report on voluntary implementation of its recommendations.

A communiqué was published following the, 19-20 March, meeting of G20 Finance Ministers and Central Bank Governors. Considering the ongoing process of financial regulatory reform, the most pertinent paragraph includes the following:

- The global financial system must remain open, resilient and supportive of growth and grounded in agreed international standards.
- We will continue to closely monitor and, if necessary, address emerging risks and vulnerabilities in the financial system.
- We welcome the finalisation of Basel III, which completes main elements of the post-crisis reforms.
- We remain committed to the full, timely and consistent implementation and finalisation of the reforms and their evaluation to help identify and address any material unintended consequences and ensure that the reforms accomplish their objectives.
- We look forward to the FSB-led evaluation of the reforms, including their effects on the financing of infrastructure investment and on incentives for CCP clearing of OTC derivatives.

An annex to this communiqué includes a list of issues for further action, including the following:

- We ask the IMF, the BIS and the FSB to present to us, at our meeting in April, a common report on financial stability risks during policy normalisation.
- We look forward to the convening of an infrastructure private sector advisory group which will provide technical advice on the infrastructure agenda in 2018.
- We ask the IMF to complete and publish its macroprudential database, in April.
- We ask the FSB, in consultation with other SSBs, including CPMI and IOSCO, and FATF to report, in July, on their work on crypto-assets.
- We ask the Sustainable Finance Study Group (SFSG) to report, by July, on the development and assessment of options for voluntary adoption by members to help deploy financing, including by creating sustainable assets for capital markets, developing sustainable Private Equity and Venture Capital, and exploring potential application of digital technologies to sustainable finance, taking into account countries' circumstances, priorities and needs.

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New opportunities to access the Chinese markets

By Wei Kong, Partner, Zhong Lun Law Firm, and Ricco Zhang, Director, Asia Pacific, ICMA

Following the update on Chinese policy developments in the last ICMA Quarterly Report, this article provides further detail about Chinese financial market regulatory reform and an update on new opportunities for international financial institutions following China's annual congress meeting held in March 2018.

China's financial regulatory regime is undergoing significant structural change. In July 2017, the Financial Stability Development Committee (FSDC) was established to strengthen the coordination of financial supervision and address gaps and overlaps in the regulation of financial markets. The Chinese Government has now taken a further step. Pursuant to the institutional reform plan issued by the State Council in March 2018, the China Banking Regulatory Commission (CBRC) and China Insurance Regulatory Commission (CIRC) will merge into a new China Banking and Insurance Regulatory Commission (CBIRC), unifying supervision of the banking and insurance industries.

These measures are intended, in particular, to (i) improve coordination among regulators and policymakers; (ii) reduce loopholes and opportunities for regulatory arbitrage; and (iii) encourage financial innovation while providing clearer accountability for systemic financial risk. It is notable that in China, life insurance has been increasingly used as an investment product, with products similar to savings products offered by banks. In addition, banks have become major distribution channels for insurance products in China.

Furthermore, with respect to institutional reform, the People's Bank of China (PBOC) will take on primary responsibility for prudential financial market supervision and will be the only regulator with the power to promulgate regulations regarding banking and insurance. The new officials appointed to head the PBOC and CBIRC have been received positively by both domestic and international markets, and are expected to ensure policy continuity, better regulatory coordination, and a further push for market-oriented reform in the financial sector in China.

During 2017, the Chinese Government also announced several regulations and laws to relax restrictions on foreign investments in banking, insurance, securities, futures, fund management and investment consulting in China.

In July 2017, CBRC revised the *Implementing Measures of the China Banking Regulatory Commission for Administrative Licensing Matters for Chinese-funded Commercial Banks*. In November 2017, the CBRC announced the *Interim Measures for the Equity Management of Commercial Banks (Draft for Comments)*. And in February 2018, CBRC updated the *Administrative Licensing of Foreign-funded Banks*. These measures are an indication of CBRC's commitment to further open up the domestic banking industry to foreign investment. In addition, the Governments of Fujian and Guangdong provinces also delivered notices to support further foreign investment in the banking industries in these provinces.

In March 2018, the China Securities Regulatory Commission (CSRC) published draft *Measures for Administration for Securities Companies with Foreign Investments*, pursuant to which foreign financial institutions could be allowed to hold a controlling number of shares of joint venture securities companies, and the limit on a single foreign investor's shares in a listed securities company could be relaxed from 20% to 30%. More draft rules are expected to be published for comment over the next few months.

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European financial regulatory reforms

On 17 January 2018, MEPs discussed the priorities of the incoming Bulgarian Presidency of the Council of the EU with Prime Minister Boyko Borissov. This Plenary Session in Strasbourg involved the first the presentation of the programme of activities of the Bulgarian Presidency. Pages 24 and 25 of this programme cover the Presidency's priorities in the sphere of the Economic and Financial Affairs Council.

In particular, this states that the Bulgarian Presidency will direct its efforts towards the completion of the Banking Union with a focus on reducing the risks in the banking sector and on developing a CMU; and will also be prioritising promoting investment, securing sustainable economic growth and guaranteeing fair competition in the Single Market.

In this context, among other things, the Presidency will:

- strive to find an acceptable balance and compromise on the legislative package for risk reduction in the banking sector;
- make progress on the proposal for the establishment of a European Deposit Guarantee Scheme;
- start the work on the other measures for completing the Banking Union outlined in the Commission's Communication of 11 October 2017;
- continue working on:
  - the discussion of the legislative proposals on clearing obligations and derivative reporting;
  - the establishment of a framework for recovery and resolution of CCPs and supervisory oversight, as well as on requirements *vis-à-vis* third-country CCPs; and
  - the legislative proposal for the creation of a pan-European pension product;
- start substantive discussions on:
  - the review of the ESFS; and
  - the proposal to introduce a new prudential regime for investment firms; and
- encourage the debate on deepening of the EMU, including in relation to the Commission's package of proposals of 6 December 2017.

In 2016, the ESRB General Board agreed that the pooling and tranching of cross-border portfolios of national sovereign bonds represents an interesting and attractive approach that could contribute to the ESRB's objectives. On this basis, the General Board commissioned a High-Level Task Force on Safe Assets, chaired by Philip R. Lane, Governor of the Central Bank of Ireland, to investigate the practical considerations relating to sovereign bond-backed securities (SBBS). On 29 January, the outcome of the Task Force's investigation was published in a report comprising two volumes. The first volume conveys the Task Force's main findings; the second contains the technical analysis underpinning those findings. In addition, the ESRB has published a series of working papers related to SBBS.

The Task Force's main finding is that a gradual development of a demand-led market for SBBS might be feasible under certain conditions. One necessary condition is for an SBBS-specific enabling regulation to provide the conditions for a sufficiently large investor base, including both banks and non-banks. To enhance financial stability, this regulation would need to treat the different tranches of SBBS according to their unique design and risk properties. For banks, regulating senior SBBS no more severely than sovereign bonds could incentivise them to hold these low-risk securities. The regulatory treatment of mezzanine and junior SBBS should reflect their greater riskiness.

In addition, the Task Force analysed how investor demand for SBBS would be affected by the regulatory treatment of sovereign exposures (RTSE). This analysis was conducted without prejudice to policy discussions on RTSE ongoing in other fora. If those discussions result in changes to the treatment of sovereign exposures to reflect credit or concentration risk, demand for senior SBBS would be substantially enhanced. Clearly, however, this finding does not provide sufficient justification for embarking upon such regulatory reform, which should be evaluated on its own merits. Ultimately, the level of investor demand for SBBS and its impact on financial markets is an empirical question, which can only be tested if an enabling regulation for the securities is adopted.

The publication of the report and working papers is intended to inform wider policy discussions on the feasibility and impact of creating a market for SBBS as a tool to enhance financial stability. On a related note, on 23 January, the European Commission published an inception impact assessment regarding an enabling regulatory framework for the development of SBBS, requesting any comments by 20 February.

On 30 January, EIOPA published its updated Work Programme for 2018, highlighting and specifying its activities and tasks for the coming year, within the framework of a multiannual work programme 2017-2019. To develop EIOPA further as a credible supervisory Authority within the ESFS it is following three main strategic priorities: (i) enhancing supervisory convergence; (ii) reinforcing preventive consumer protection; and (iii) preserving financial stability.

On 7 February, ESMA published its 2018 Supervisory Convergence Work Programme (SCWP), which details the activities and tasks it will carry out to promote sound, efficient and consistent supervision across the EU. The SCWP 2018 sets priorities that will drive ESMA's convergence agenda in the year

ahead and foster coordinated action by national securities and markets supervisors. While many of the 2017 priorities remain relevant for 2018, ESMA also sets new priorities, notably in the areas of financial innovation and the UK's withdrawal from the EU.

For 2018, ESMA has identified the following priorities for supervisory convergence:

- ensuring that MiFID II/MiFIR are applied in a sound, efficient and consistent manner across the EU (continuous);
- improving data quality to ensure efficient reporting under various requirements set by EU legislation (continuous);
- ensuring supervisory convergence in the context of the UK's decision to withdraw from the EU (new);
- safeguarding the free movement of services in the EU through adequate investor protection in the context of cross-border provision of services (continuous); and
- monitoring developments in financial innovation, in particular through the analysis of emerging and existing instruments, platforms and technology (new).

Subsequently, on 8 February, ESMA published its 2018 Supervision Work Programme setting out its main supervisory activities for CRAs, trade repositories (TRs), and third country CCPs in the EU.

Additionally, on 7 February, also elaborating on its 2018 Work Programme (published on 5 October 2017), ESMA published its 2018 Regulatory Work Programme. This lists 48 different 2018 annual work programme sub-activities, comprising 14 re the Prospectus Regulation; 10 re the STS Securitisation Regulation; 13 re EuSEF, EuVECA and ELTIFs; two each re SFTR, MiFID and EMIR; four re MAR; and one re Benchmarks Regulation.

Completing the elaboration of its 2018 Work Programme, on 9 February, ESMA published its Risk Assessment Work Programme, setting out its priorities in assessing risks for securities markets for 2018. As market data collected under the AIFMD, MiFID and EMIR mandates and others are becoming available, ESMA is – in close cooperation with the NCAs – completing the necessary technical infrastructure for their processing, programming routines for their management, and making them available for the relevant analytical evaluation. ESMA will further enhance its risk monitoring capacities, generating market descriptive statistics as well as sophisticated risk indicators and metrics on the basis of new proprietary data.

Most importantly for 2018, ESMA is planning to complement its ongoing market monitoring through its semi-annual *Report on Trends, Risks and Vulnerabilities* and its quarterly *Risk Dashboards* by launching an annual report series on EU derivatives markets, based on EMIR data, as well as an annual report series on EU alternative investment funds, drawing on AIFMD data. In addition, ESMA will continue to pursue in-depth analyses around key topics, including market and fund liquidity, fund leverage and the impact of innovation, especially in the areas of market infrastructures and investment advice.

On 8 February, the European Commission published seven notices to stakeholders, setting out the consequences that the UK withdrawal from the EU will have on banking and finance rules. Specifically, these notices cover rules in the fields of: (i) markets in financial instruments; (ii) banking and payment services; (iii) post-trade financial services; (iv) asset management; (v) credit rating agencies; (vi) insurance / reinsurance; and (vii) statutory audit.

On 8 March, on the basis of the recommendations set out by the High Level Expert Group on sustainable finance (HLEG), the European Commission set out a roadmap to boost the role of finance in achieving a well-performing economy that delivers on environmental and social goals as well. This Action Plan on sustainable finance is part of the CMU's efforts to connect finance with the specific needs of the European economy to the benefit of the planet and our society.

Alongside this, the European Commission also unveiled an Action Plan on how to harness the opportunities presented by technology-enabled innovation in financial services (FinTech), with the aim of making Europe a global hub for FinTech, again as a part of the Commission's efforts to build a CMU and a true single market for consumer financial services; and as a part of its drive to create a Digital Single Market. As a first major

ESMA will continue to pursue in-depth analyses around key topics, including market and fund liquidity, fund leverage and the impact of innovation.

deliverable, the Commission also put forward new rules intended to help crowdfunding platforms to grow across the EU's Single Market.

Furthermore, also on 8 March, the European Commission published a Communication, *Completing the Capital Markets Union by 2019 – Time to Accelerate*. The Commission is committed to put in place all building blocks of CMU by mid-2019. While first achievements and major milestones have already been reached (see table in annex), the Commission believes it is now the time to move ahead and make sure that all pending legislative proposals are completed by the end of the mandate.

To this end, the Commission has proposed the further measures outlined in the previous paragraph to develop and integrate EU capital markets; and the remaining proposals will be presented by May 2018 so that, with the necessary political will, legislation can be adopted before the European Parliament elections in 2019. Going forward, the Commission aims to give a strong impetus to the effective functioning of CMU, by placing the building blocks around three mutually reinforcing dimensions: the EU Single Market; clear and proportionate rules; and efficient supervision.

On 12 March, the European Commission outlined further steps being taken towards the development of CMU, by promoting alternative sources of financing and removing barriers to cross-border investments. Steps were elaborated in three areas:

1. common rules, consisting of a Directive and a Regulation, for covered bonds, which represent an important source of long-term financing in many EU Member States – these proposed rules are based on high-quality standards and best practices;
2. proposals to remove regulatory barriers that currently hinder the cross-border distribution of investment funds, making cross-border distribution simpler, quicker and cheaper; and
3. new rules to clarify which national law applies when determining disputes regarding who owns a claim after it has been assigned in a cross-border case – as a general rule, the law of the country where assignors have their habitual residence would apply, regardless of which Member State's courts or authorities examine the case. And, alongside this, the Commission also adopted a Communication to clarify which country's law applies when determining who owns a security in a cross-border transaction.

The Vienna Initiative announced that it has now set its sights on a growth model for the region that drives forward innovation and boosts productivity. At a full forum meeting of the Vienna Initiative, in London on 12 March, participants also gave their backing for plans to bolster capital markets in the central, eastern and south-eastern Europe (CESEE) region.

These proposals are set out in a new report, produced by the Working Group on CMU, chaired by the European Commission, which makes a thorough analysis of capital markets throughout the CESEE region; assesses the key main challenges for capital market development in selected CESEE countries; and offers policy recommendations aimed at realising the potential of local markets in the EU context. The Commission plans to publish a related Communication.

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Financial benchmarks

On 12 January 2018, EMMI announced that it remains committed towards EURIBOR compliance with the EU Benchmarks Regulation (BMR). EMMI is pursuing efforts to finalise and test a reformed methodology which will better reflect the underlying interest it intends to measure and adapt to the prevailing market conditions. In particular, it will be anchored on actual market transaction input data whenever available and on other funding sources if transaction data are insufficient.

EMMI aims to launch the hybrid methodology for EURIBOR by Q4 2019 at the latest, in accordance with the transitional period provided by the BMR. EMMI is also strengthening the governance framework and the benchmark setting process in alignment with ESMA's draft RTS.

Subsequently, in early February, EMMI published a statement regarding the *State of Play of the EONIA Review*. This highlights that it is not proceeding with work to reform EONIA. EMMI confirms that the daily publication of EONIA will continue "as-is", and highlights that, following the BMR, EONIA may still be used as a reference rate until 31 December 2019 (under the transitional provisions). Further, after 1 January 2020, the provision and use of EONIA in existing contracts may be permitted by the FSMA, under the conditions set out in Article 51(4) BMR.

Nonetheless, in line with benchmark users' responsibilities foreseen in the BMR, EMMI encourages users to assess whether their selected benchmarks meet their, or their clients', needs – both upon initial selection and in ongoing use. In addition to assessing the appropriateness of the selected benchmarks, users should give careful thought to contingency plans in the event a benchmark is no longer available (ie users should seek to put in place fall-back provisions in their contractual arrangements).

As reported in this section of Issue 48 of the ICMA Quarterly Report, the FSMA, ESMA the ECB and the European Commission had sought expressions of interest to participate

in a Working Group on Euro Risk-Free Rates. The composition of this group, including ICMA as a non-voting member, was subsequently announced and the group's inaugural meeting was held, on 26 February, hosted by the ECB in Frankfurt. To drive work forward in a timely fashion, it was agreed that there should be three work streams: a work stream #1 covering the choice of alternative risk-free rates; a work stream #2 exploring the construction of term rates; and a work stream #3 investigating contractual robustness for both legacy and new contracts indexed to the existing benchmarks.

Alongside this, the ECB's Governing Council has decided to develop a daily euro unsecured overnight interest rate, based on data already available to the Eurosystem. This will be finalised before 2020, will complement existing benchmark rates produced by the private sector and will serve as a backstop to private-sector benchmark rates. A first public consultation, which ended on 12 January, was held to gather feedback on the high-level features of the new rate. Subsequently, a second public consultation was launched, on 15 March (for comments by 20 April) to gather feedback on the defined methodology of the new rate, as well as on key operational and technical parameters.

The Bank of England is currently in the process of reforming the SONIA benchmark, with the reforms set to become effective on 23 April. The changes are: (i) the Bank will produce SONIA, including the calculation and publication as well as being the SONIA administrator; (ii) SONIA will be broadened to include overnight unsecured transactions negotiated bilaterally as well as those arranged via brokers; (iii) the averaging methodology for calculating SONIA will change to a volume-weighted trimmed mean; and (iv) SONIA will be published at 9 am on the business day following the day the rate relates to, allowing time to process the larger volume of transactions it will capture.

The Bank and the UK FCA are working with market participants to catalyse a transition to SONIA in sterling markets.

Consistent with the selection of reformed SONIA as the sterling risk-free reference rate, the Bank and the UK FCA are working with market participants to catalyse a transition to SONIA in sterling markets.

On 13 March, it was announced that ICE Benchmark Administration Limited (IBA) would publish data relating to a three-month testing period, between 15 September and 15 December 2017, during which all 20 LIBOR panel banks were required to make parallel LIBOR submissions. These parallel submissions used the evolved waterfall methodology set out in the ICE LIBOR output statement; and IBA has calculated LIBOR for each of the 35 LIBOR currency and tenor pairs, for every applicable London business day of the testing period, applying the same trimmed arithmetic mean approach used to calculate LIBOR as it is currently published.

IBA continues to work on the evolution of LIBOR, with the intention of transitioning panel banks from the existing LIBOR methodology to the waterfall methodology, subject to agreement from the LIBOR Oversight Committee, IBA approvals, other approvals and steps as necessary or appropriate, and the absence of regulatory objection.

On 14 March, the UK FCA published *PS18/5: Powers in Relation to LIBOR Contributions*. This policy statement sets the approach, criteria and methodology that the FCA proposes to apply if it needed to use powers to compel banks to contribute to LIBOR.

Published on 23 March, in the Bank of England's Quarterly Bulletin Q1 2018, *Sterling Money Markets: Beneath the Surface* is an article, authored by staff in the Bank's Markets Directorate, which presents analysis based on the Bank's new Sterling Money Market data collection. The vast majority of unsecured money market activity is in the overnight market that underlies the SONIA benchmark, with longer-maturity trades being scarce and having volatile daily average interest rates. The authors present evidence that suggests the overnight unsecured market is dynamic and competitive; and show that average rates in the overnight gilt repo market vary according to the collateral used. These observations support market-led efforts to promote the use of SONIA in sterling markets.

On 5 March, the US Alternative Reference Rates Committee (ARRC) released its *Second Report*; and on 7 March the Federal Reserve Board and the Federal Reserve Bank of New York announced that the ARRC has been reconstituted.

EMMI published a first consultation paper, dated 26 March, on a hybrid methodology for EURIBOR.

For comment by 15 May, this consultation presents a proposed methodology, composed of a three-level waterfall, which leverages on market transactions whenever available, and provides further details on the determination of each level respectively. In addition, EMMI seeks to gather the market's views on certain features of the current publication process, as well as on other aspects, such as the inclusion and/or cessation of certain tenors. This consultation is a first step to be followed by an in-depth testing of the proposed methodology under live conditions from May to August 2018. A second consultation providing further details on certain parameters is scheduled for Q3 2018, whilst EMMI proceeds towards launching of the hybrid methodology by Q4 2019 at the latest.

The text of the BMR, which was published in the *Official Journal* on 29 June 2016 and entered into force the following day, entered into full application on 1 January 2018. 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 of the BMR. The first version of ESMA's BMR Q&A document was published on 5 July 2017, with the most recent update having been published on 22 March.

On 19 December 2017, ESMA issued an announcement that it would, as from 3 January (ESMA's first working day of 2018), begin publishing a register of administrators and third country benchmarks, in accordance with Article 36 of the EU Benchmarks Regulation. ESMA is currently still working on a new technical release of this register. Therefore, until the new register release is fully available as an IT functionality on its website (in Q3 2018), ESMA will provide an interim solution which involves it publishing, on a daily basis (ESMA working days), the latest registers' information in a comma-separated values (CSV) file format, available for download.

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Credit rating agencies

On 11 January 2018, ESMA published a *Thematic Report on Fees Charged by Credit Rating Agencies (CRAs) and Trade Repositories (TRs)*, following the conclusion of ESMA's supervisory review of the current fee structures in the CRA and TR industries. Based on collated review evidence, this report provides ESMA's views on the application of the requirements that fees charged by CRAs should be non-discriminatory and cost-based, and TRs provide non-discriminatory access and charge publicly disclosed and cost-related fees. It equally identifies the areas for improvement regarding transparency and disclosure, the fee-setting process and the interaction with entities related to CRAs and TRs. Going forward, these areas will form the core of ESMA's supervisory focus.

The three main areas that raise supervisory concerns are:

1. *Transparency and disclosure:* CRAs/TRs need to ensure sufficiency and clarity of information provided to actual and potential clients as well as to ESMA;
2. *Fee-setting process:* CRAs/TRs need to ensure that cost is a key pricing factor and sufficient controls are in place to demonstrate that the regulatory objectives regarding pricing are met; and
3. *Interaction with entities related to CRAs and TRs:* CRAs need to ensure that provision of rating-related services by affiliated entities does not conflict with the non-discrimination and cost-based principles; and TRs that are part of a group need to ensure that intra group transactions are on reasonable terms and on an arm's-length principle.

On 8 February, ESMA published its 2018 Supervision Work Programme setting out its main supervisory activities for CRAs, trade repositories (TRs), and third country CCPs in the EU. ESMA supervises eight registered TRs, 26 registered CRAs and four certified CRAs from third-countries. The report also details ESMA's supervisory activities and achievements in 2017.

Published on 16 February, *Are Credit Rating Agencies Discredited? Measuring Market Price Effects from Agency Sovereign Debt Announcements* is a BIS staff working paper. The authors look at whether the information value of CRA announcements relating to sovereign bonds has diminished since the Global Financial Crisis (GFC) of 2007-09. In particular, taking into account the prior credit status of the bonds, they measure how the response of CDS spreads to such announcements has changed. Overall, they find that upgrades and downgrades from a stable/developing status exhibit the strongest market responses. By contrast, the responses are weakest when the bonds are already under watch. Following the GFC, announcements continued to have statistically significant impacts on CDS spreads, although such impacts were substantially less pronounced for most announcement categories.

ESMA announced that it has registered SPMW Rating Sp. z o.o. as a CRA under the CRA Regulation), with effect from 15 March. SPMW Rating Sp. z o.o. is based in Poland, issuing sovereign and public finance ratings and corporate ratings. This registration increased the total number of CRAs registered in the EU to 27 – amongst which three operate under group structures, totalling 17 legal entities in the EU, which means that the total number of CRA entities registered in the EU is 41.

On 27 March, ESMA published a consultation paper (for comment by 25 May) with proposed supplementary guidance on the application of the endorsement regime in the EU's CRA Regulation (CRAR). The aim of the proposed supplementary guidance is twofold: (i) to provide clarity regarding the general principle ESMA relies on when assessing whether an alternative requirement can be considered as stringent as a requirement set out in the CRAR; and (ii) ESMA's concrete assessment of a number of alternative internal requirements which are currently in place in a third-country CRA. The consultation paper proposes to add the supplementary guidance as an additional subsection of ESMA's updated Guidelines on Endorsement which will apply to credit ratings issued after 1 January 2019 or reviewed after that date.

On 20 November 2017, ESMA published the most recent update to its Q&A on the application of the EU CRA Regulation.

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ESMA's guidelines provide details on circumstances where conflicts of interest could arise and specifies the corresponding organisational arrangements and procedures to be set up.

OTC (derivatives) regulatory developments

On 2 February 2018, ESMA published the results of its second EU-wide stress test exercise regarding CCPs established in the EU. This CCP stress test assesses the resilience and safety of the EU CCP industry and helps to identify possible vulnerabilities. These results show that overall the system of EU CCPs is resilient to multiple clearing member (CM) defaults and extreme market shocks. In addition, the report also highlights individual CCP-specific results.

The stress test builds on the first CCP stress test conducted in 2016, which focused on counterparty credit risk only, with the second exercise including liquidity risks – examining whether CCPs would meet their liquidity needs under different stress scenarios. ESMA tested the resilience of 16 European CCPs with approximately 900 CMs EU-wide.

On 7 February, ESMA issued final guidelines on the management of conflict of interests for CCPs. Under EMIR, CCPs have to put in place organisational arrangements and policies to prevent potential conflicts of interest and to solve them if the preventive measures are not sufficient. In order to ensure a level playing field across the EU, ESMA decided to develop guidance on CCPs management of conflicts of interests. ESMA's guidelines provide details on circumstances where conflicts of interest could arise and specifies the corresponding organisational arrangements and procedures to be set up, including in the case when a CCP is part of a group structure. Each NCA will have to confirm whether or not it intends to comply with the guidelines.

Published on 13 March, *Clearinghouse-Five: Determinants of Voluntary Clearing in European Derivatives Markets* is an ESRB working paper. The author uses a dataset of all newly entered into derivatives contracts in the EU between March 2016 and June 2017 to show the extent to which CCP clearing is being used for derivatives belonging to all five major asset classes, and to determine which characteristics of the contracts not under the clearing obligation a ect the likelihood they would be voluntarily CCP cleared. He shows that currently only around 20% of credit and 40% of interest rate derivatives are CCP cleared, while equity, FX, and commodity derivatives are barely CCP cleared; and that there are significant e ects of scale connected with CCP clearing, both in terms of previous clearing activity of the counterparty and the notional of the specific contract.

Published on 20 March, *Central Counterparties Resolution – An Unresolved Problem* is an IMF staff working paper. The authors analyse current resolution tools in the context of policy, which is to restore the critical functions of a failed CCP. They conclude that the toolkit is insufficient to avoid the costs of resolution being borne by taxpayers and propose alternative policy suggestions for addressing the problem of a failed CCP. Some of those would demand that regulators accept that the existing policy belief – in particular, that mandatory clearing must carry on under all circumstances – may not hold valid in a crisis.

Ten years after the global financial crisis, granular big data are becoming increasingly available to policy makers

in order to improve the transparency and understanding of financial markets. EMIR requires transaction-level data on derivatives contracts to be reported to TRs and grants the ESRB access to the EU-wide dataset - the full dataset consists of approximately one hundred million observations per day.

To exploit the wealth of information from this newly available dataset, the ECB and ESRB are running the EMIR Bridge Programme for Data Science, which aims to develop novel analytical methods and to foster interaction between the policymaking and research communities. In a first step they are conducting a market survey with the aim of exploring and initiating collaboration opportunities with potentially interested parties.

On 23 March, the FSB announced that it is seeking responses from financial institutions and other reporting entities on issues they may face with legal barriers to the reporting of full transaction information about OTC derivatives. The requested responses will provide input to the FSB's ongoing work to evaluate the extent to which its member jurisdictions have met their commitments to remove such legal barriers; and the FSB will report on the findings to the G20 Summit in Buenos Aires. Such barriers may arise from client confidentiality, data protection, blocking statutes, or other official requirements, either in FSB member jurisdictions or other jurisdictions where counterparties may be located.

On 27 March, ESMA published guidelines on how TRs should calculate derivative positions under EMIR, a consistent approach to which is crucial for the assessment of systemic risks to financial stability. TRs should follow these guidelines to ensure that they produce consistent and harmonised position calculations for public authorities, such as conduct regulators, central banks, prudential and resolution authorities. The guidelines will be translated into the official languages of the EU and become applicable by 3 December 2018.

Published on 29 March, *Indicators for the Monitoring of Central Counterparties in the EU* is an ESRB occasional paper, which complements the publication of indicators on CCPs in the ESRB's Risk Dashboard as part of its monitoring framework. It provides a methodological background to the development of the individual measures and discusses different aspects that should be considered when designing a monitoring framework for CCPs. The paper also highlights a number of areas in which more granular data are required in order, for example, to monitor the interconnectedness of CCPs within the broader financial system.

ESMA's list of CCPs authorised to offer services and activities in the EU, in accordance with EMIR, was last updated on 18 January, as was its list of third-country CCPs recognised to offer services and activities in the EU. ESMA's *Public Register for the Clearing Obligation* under EMIR was last updated on 19 January; whilst its (non-exhaustive) list of CCPs established in non-EEA countries which have applied for recognition has not been updated since 18 April 2017.

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 5 February.

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FinTech regulatory developments

BCBS Sound Practices

On 19 February 2018, the Basel Committee on Banking Supervision (BCBS) published a report on *Sound Practices: the Implications of FinTech Developments for Banks and Bank Supervisors*. The paper assesses how technology-driven innovation in financial services, or "FinTech", may affect the banking industry and the activities of supervisors in the near to medium term. The paper focuses on three technological developments (big data, distributed ledger technology and cloud computing) and three FinTech business models (innovative payment services, lending platforms and neo-banks).

European Commission FinTech Action Plan

On 8 March 2018, the European Commission released its FinTech Action Plan for a more competitive and innovative European financial sector. It envisages to enable the financial sector to make use of the rapid advances in new technologies, such as blockchain, artificial intelligence and cloud services. At the same time, it seeks to make markets safer and easier to access for new players.

The FinTech Action Plan is part of the Commission's efforts to build a Capital Markets Union (CMU) and a true single market for consumer financial services. It is also part of its drive to create a Digital Single Market. The Commission aims to make EU rules more future-oriented and aligned with the rapid advance of technological development. The Commission sets out 19 steps to enable innovative business models to scale up, support the uptake of new technologies, increase cybersecurity and the integrity of the financial system.

ESAs Joint Committee Final Report on Big Data

On 15 March 2018, the Joint Committee of the European Supervisory Authorities (ESAs) published its *Final Report on Big Data,* analysing its impact on consumers and financial firms. Weighing both the benefits and the risks associated with this innovation, the ESAs have concluded that any legislative intervention at this point would be premature, considering that the existing legislation should mitigate many of the risks identified. The ESAs will continue to monitor any developments in this area in the coming years and invite financial firms to develop and implement good practices on the use of Big Data.

EBA FinTech Roadmap

On 15 March 2018, the European Banking Authority (EBA) published a *FinTech Roadmap* setting out its priorities for 2018/2019 in light of the feedback received and in alignment with the European Commission's FinTech Action Plan. This includes:

- monitoring the regulatory perimeter, including assessing current authorisation and licencing approaches to FinTech firms, analysing regulatory sandboxes and innovation hubs with a view to developing a set of best practices to enhance consistency and facilitate supervisory coordination;
- promoting best supervisory practices on assessing cybersecurity and promoting a common cyber threat testing framework;
- identifying and assessing money laundering/terrorist financing risks associated with regulated FinTech firms, technology providers and FinTech solutions.

The Roadmap also sets out the establishment of a FinTech Knowledge Hub to enhance knowledge sharing and foster technological neutrality in regulatory and supervisory approaches.

FCA global regulatory sandbox

On 14 February 2018, the UK Financial Conduct Authority (FCA) announced it was considering the launch of a global regulatory sandbox. Feedback was sought from market stakeholders "on the merits of creating a global sandbox. This could potentially allow firms to conduct tests in different jurisdictions at the same time and allow regulators to work together and identify and solve common cross-border regulatory problems, through tests. Under such a model, testing could span two or more jurisdictions." Based on the feedback received, the FCA is due to publish a further update.

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Market infrastructure

ECB: TARGET2-Securities (T2S)

Around six months after the successful completion of the final T2S migration wave in September 2017, the platform now processes over 600,000 transactions a day with an average daily value of close to €650 billion, as the latest T2S operations update shows (February 2018). Settlement efficiency continues to be consistently high, at close to 98% both in terms of volume and value. However, the experience so far has not been all bright. T2S settlement volumes remain significantly lower than initially estimated, especially cross-CSD settlement, and users are still challenged to extract real value from the new settlement environment. Particularly from a front-office perspective, T2S has so far failed to make a substantial difference as discussions with users indicate (see, for example, the article on the ERCC AGM in the Repo and Collateral Section of this Quarterly Report). This clearly shows that the successful completion of the technical part of the T2S project is only the first step in a much longer process towards a more integrated settlement environment in Europe.

One of the key positive achievements of T2S has been, without a doubt, the extensive harmonisation agenda that has accompanied the project.

One of the key positive achievements of T2S has been, without a doubt, the extensive harmonisation agenda that has accompanied the project. The 8th and latest *T2S Harmonisation Progress Report*, published on 31 January, shows that a lot has been achieved on this front. The report now indicates an overall compliance level of 85% with the 16 harmonisation standards that have been deemed of highest priority, up from 70% at the time of the previous mid-year report. Most significant gaps remain in the field of corporate actions.

On 6 March, all national central banks jointly operating TARGET2 systems and all CSDs participating in T2S signed a collective agreement on the provision of information and liability in the event of a participant in their systems becoming insolvent. The agreement defines a common moment of entry of a transfer order into the system ("Settlement Finality 1") and is hence another important step in terms of T2S harmonisation.

ECB: Advisory Groups on market infrastructure

The AMI-SeCo, which brings together Eurosystem, user community and the relevant market infrastructure providers, had its latest meeting on 20 March in Frankfurt. This was the fourth meeting of the group in which the ICMA ERCC is represented through ERCC Ops co-chair, Nicholas Hamilton (this time substituted by Adam Bate, his fellow co-chair). During the latest meeting, ESMA and the Commission provided updates on their work in relation to the broader post-trade harmonisation agenda and the status of the various relevant regulatory initiatives that are still under way (see details below). Another key focus of the meeting was on harmonisation, both directly related to T2S and in relation to the complementary work that has been launched on collateral management (see separate section below). The third block of discussion was related to T2S operations and feedback from the different T2S governance groups. Importantly for T2S users, this included a preliminary discussion on an upcoming review of the T2S pricing schedule. This will be discussed more in-depth at a dedicated workshop on this topic which will be held on 17 May. As usual, all related meeting documents are available on the ECB website. The next regular AMI-SeCo meeting is scheduled for 21-22 June.

The ECB's second market infrastructure related advisory group, AMI-Pay, has not had a regular meeting this year so far. However, the group met on 6 February for an *ad hoc* meeting focused on instant payments and the TARGET Instant Payment Settlement (TIPS) service which is being developed by the ECB (see below). The next regular AMI-Pay meeting is scheduled for 17 April.

ECB: collateral management harmonisation

In December 2017, the ECB Governing Council approved a plan to develop a Eurosystem Collateral Management System (ECMS). With the ECMS the ECB aims to offer a single system for users to manage eligible assets used as collateral for Eurosystem credit operations, replacing the currently still fragmented collateral framework based on the Correspondent Central Banking Model (CCBM). A Eurosystem

internal Working Group was established in February 2018 to work on the technical details of the solution ahead of the scheduled "go-live" in 2022. An overview of the project and the implementation timeline is included in the latest ECMS update to AMI-SeCo.

Complementing the ECMS project, detailed work is being undertaken to harmonise processes and market practices in relation to collateral management more broadly. The initiative is coordinated by AMI-SeCo, but the detailed work is undertaken by a dedicated Collateral Management Harmonisation Task Force (CMH-TF), which is comprised of industry experts, including from the ICMA ERCC. The CMH-TF has established five workstreams on the different aspects covered by the harmonisation agenda, including triparty models, bilateral business and margining or corporate actions. The latest CMH-TF status update to AMI-SeCo provides a good overview of progress achieved to date and the next steps for the group.

Detailed work is being undertaken to harmonise processes and market practices in relation to collateral management more broadly.

ECB: Other market infrastructure-related initiatives

Besides collateral management, the Eurosystem is working on a number of further market infrastructure related initiatives, all of which are closely coordinated with market participants through the two advisory groups, AMI-SeCo and AMI-Pay.

One important project is the consolidation of the TARGET2 and the T2S platforms. In December 2017, following two public consultations on the project and the detailed user requirements, the initiative received the green light from the ECB's Governing Council. In January 2018, a TARGET consolidation contact group was created to work out the details of implementation and advise on user testing, migration and change management activities.

A second initiative is the TARGET Instant Payment Settlement (TIPS) service which is scheduled to go live in November 2018. A dedicated TIPS contact group was established in July 2017, following final approval by the ECB Governing Board, to work out the details. The latest development in this context was the so-called #TIPSapp challenge, a call issued by the ECB for commercial providers to develop a user-friendly mobile app for initiating and processing instant payments. The 16 providers that responded to the call had a chance to present their solutions at a #TIPSapp event on 6 February in Frankfurt. More information on the event and the challenge is available on the ECB website.

The ECB also continues to monitor closely developments related to FinTech, in particular the potential implications of emerging Distributed Ledger Technology (DLT) for current infrastructure arrangements and the post-trade integration in Europe more broadly. In July 2016, a dedicated DLT Task Force was created, which subsequently worked on a detailed report on this question which was published in September 2017. Since then, members of the Task Force have identified a number of follow-up actions for the group which are now being addressed, as reflected in the Task Force's latest update to AMI-SeCo.

On 27 March 2018, the ECB and the Bank of Japan published the findings of the second phase of the joint research project "Stella", which studies the possible use of distributed ledger technology (DLT) for financial market infrastructures. The project explored how the delivery of securities against cash could be conceptually designed and operated in a DLT environment. It draws on existing delivery-versus-payment (DvP) approaches as well as innovative solutions that are currently being discussed for DLT. In order to gain practical understanding of DvP functioning on DLT, prototypes were developed using three DLT platforms: Corda, Elements and Hyperledger Fabric.

ECB: Market contact groups

The Bond Market Contact Group (BMCG) last met on 6 February in Frankfurt. Members discussed the bond market outlook for the year ahead, based on an introductory presentation by Wellington Management. Furthermore, members also took stock of the first weeks following MiFID II/R "go-live" in January, supported by three presentations by Morgan Stanley, Tradeweb and Union Investment. Another topic on the agenda was benchmark reform, introduced by Barclays and AFME. Finally, and most

importantly from an ICMA perspective, BMCG members also received an update on the latest developments in relation to Green and Social Bonds, provided by ICMA CEO Martin Scheck supported by Nicholas Pfaff, Senior Director at ICMA. The next regular meeting of the BMCG is scheduled for 26 June.

Members of the Money Market Contact Group (MMCG) last met on 13 March in Frankfurt. The meeting agenda included discussions on the following: (i) the evolution of market expectations for the ECB monetary policy actions; (ii) review of structural developments in the FX swap market and the USD funding of European banks; (iii) functioning of the euro area repo market: main drivers behind recent developments and rising repo volumes, and (iv) update on money market benchmarks and the working group on euro risk-free rates. The related presentations will be available in due course on the ECB website. The next quarterly meeting of the MMCG will be held on 7 June.

European Commission

In August 2017, the European Commission issued a consultation paper on remaining barriers to post-trade in Europe. All 58 responses received from stakeholders, among which there is a contribution submitted by the ICMA ERCC, have been published on the Commission's website. The consultation was issued as a follow-up to the work of the European Post Trade Forum (EPTF) in which ICMA was represented as a member. In terms of next steps, taking into account feedback received in response to the consultation, the Commission is expected to issue a Communication in Q3 2018 setting out concrete next steps towards a more harmonised and integrated European post-trade environment.

In the meantime, some progress is already being made on of certain issues identified in the final EPTF report. In particular, in December 2017, the Commission published a (non-binding) Code of Conduct to increase the efficiency of withholding tax procedures across Europe. The publication of the Code was followed up by a public hearing held on 31 January. Further meetings will be organised in the course of 2018 to monitor experiences with and potential obstacles to the implementation of the Code.

Another important issue that is being considered in this context is the harmonisation of conflict of laws provisions. On 7 March, the Commission published a legislative proposal to introduce common conflict of laws rules on claims (proprietary effects of cross-border assignments of claims). This was accompanied by a Communication clarifying existing conflict of laws rules with regard to securities (proprietary effects of transactions) which aims to complement the relevant EU Directives on this issue.

Finally, the EPTF report discussed in some length unnecessary complexities and inconsistencies across existing supervisory reporting regimes in the EU. As work on some of the legislative proposals, eg SFT Regulation, is still ongoing the Commission is conducting a broad review of all existing EU financial reporting regimes, the so-called fitness check on supervisory reporting. The related public consultation was launched on 1 December 2017 and closed on 14 March 2018. In total, 381 responses were submitted by stakeholders and will be published on the consultation website in due course. Based on the feedback the Commission will determine whether there are potential opportunities for streamlining the various regimes.

ESMA: Post-trading

While the final technical standards in relation to the CSDR settlement discipline provisions are still pending approval (as separately described in the Repo and Collateral Markets section of this Quarterly Report), ESMA is working on the implementation of the finalised aspects of the law. Besides technical standards this also includes guidelines on a wide range of issues. Most recently, on 28 March, ESMA published final translated versions of three sets of guidelines related to CSD supervision. National competent authorities have three months from the publication date to notify ESMA whether they intend to comply with these recommendations. On 28 March, ESMA also published final guidelines on how to report internalised settlement under CSDR. Such reporting will be required from

The Commission is expected to issue a Communication in Q3 2018 setting out concrete next steps towards a more harmonised and integrated European post-trade environment.

custodians and other settlement internalisers starting from 12 September 2019. As part of the implementation measures, ESMA also maintains detailed Q&As to clarify arising implementation questions in relation to CSDR, the latest update of which was published on 26 March.

In the meantime, national competent authorities are busy assessing the CSDs' applications for authorisation under the new framework. In January 2018, VP Securities, the Danish CSD, became the second CSD to be granted authorisation by their competent authority. The full register of CSDs authorised under CSDR is available on the ESMA website.

As reported previously, ESMA recently consulted on future guidelines on the calculation of derivative positions by TRs authorised under EMIR. On 27 March, taking into account feedback received in response to the consultation, ESMA published the final guidelines which provide specific instructions on the aggregation of certain data fields and how those should be calculated by TRs prior to the provision of the data to relevant authorities. These will become applicable on 3 December.

Global Legal Entity Identifier System (GLEIS)

The MiFID II/R "go-live" in Europe has created a major push for the issuance of LEIs as a result of the strict approach taken in relation to the identifier. Since the implementation date in January, the number of LEIs issued has continued to grow at a fast pace, with now well over 1.1 million LEIs issued around the globe. The full LEI database continues to be accessible on the website of the Global LEI Foundation (GLEIF) through the free LEI search tool.

On 8 February, GLEIF and SWIFT announced that they have developed the first open source BIC-to-LEI mapping. The document which has been developed and maintained by SWIFT and certified by GLEIF aims to enable interoperability across multiple ID platforms and can be downloaded for free from the GLEIF website.

The GLEIF issues a regular and more detailed overview of LEI news, the latest edition of which was published on 30 January.

BIS: Committee on Payments and Market Infrastructures (CPMI)

On 16 February, the CPMI published a report on *Cross-Border Retail Payments*. The report finds that while several important innovations have made cross-border payments more convenient, the key to making these payments faster and cheaper is better choice and diversity of clearing and settlement arrangements.

On 19 March, during their latest Global Economy Meeting (GEM) held in Buenos Aires, CPMI Governors agreed to admit the central banks of Argentina, Indonesia and Spain to the Committee. This is the first expansion of membership since 2009. The CPMI now includes 28 members, among which representatives from all G20 countries.

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Macroprudential risk

Published on 15 January 2018, *Macroprudential Regulation in the European Union in 1995-2014: Introducing a New Data Set on Policy Actions of a Macroprudential Nature* is an ECB staff working paper. This paper introduces a new comprehensive data set on policies of a macroprudential nature in the banking sectors of the 28 EU member states between 1995 and 2014.

The Macroprudential Policies Evaluation Database (MaPPED) offers a detailed overview of the "life-cycle" of policy instruments which are either genuinely macroprudential or are essentially microprudential but likely to have a significant impact on the whole banking system. It tracks events of the introduction, recalibration and termination of eleven categories and 53 subcategories of instruments. Analytical results indicate that there has been a remarkable variation in the use of policies of a macroprudential nature, both across EU countries and over time.

On 16 January, the EBA published its regular *Risk Dashboard*. Using quantitative risk indicators, along with the opinions of banks and market analysts from its Risk Assessment Questionnaire, the EBA's dashboard identified ongoing improvements in the repair of the EU banking sector but also residual risks in NPLs and profitability. The figures included in this *Risk Dashboard* are based on a sample of 152 banks, covering more than 80% of the EU banking sector (by total assets), at the highest level of consolidation, while country aggregates may also include large subsidiaries.

Published on 23 January, *Friend or Foe? Cross-Border Linkages, Contagious Banking Crises, and "Coordinated" Macroprudential Policies* is an IMF staff working paper, which examines whether the coordinated use of macroprudential policies can help lessen the incidence of banking crises. It is well-known that rapid domestic credit and house price growth positively influence the chances of a banking crisis. As well, a crisis in other countries with high trade and financial linkages raises the crisis probability. However, whether such "contagion effects" can operate to reduce crisis probabilities when highly linked countries execute macroprudential policies together has not been fully explored. A dataset documenting countries' use of macroprudential tools suggests that such a "coordinated" implementation of macroprudential policies across highly-linked countries can help to

Many banks directly affected by the crisis have shifted their businesses away from complex and trading activities and have become more selective in their international activities.

stem the risks of widespread banking crises, although this effect may take some time to materialize.

On 24 January, the CGFS published a new report, *Structural Changes in Banking After the Crisis*, which outlines common trends but also differences across 21 countries. The banking system data, spanning the years 2000-16, are published alongside the report as a comprehensive reference tool. The report finds that, since the crisis, banks have significantly strengthened their capital and liquidity buffers, as well as their funding structures, in line with the intended direction of regulatory reforms. A stronger banking sector now generally supports the flow of credit to the real economy, although conditions vary across the globe.

Many banks directly affected by the crisis have shifted their businesses away from complex and trading activities and have become more selective in their international activities. In contrast, banks less affected by the crisis, including those in many emerging markets, have expanded internationally. The decline in bank return-on-equity from historically high pre-crisis rates partly reflects lower leverage and risk-taking, but also sluggish revenues and high costs. Longer-term profitability challenges could also signal overcapacity and the need for further structural adjustment supported by robust bank resolution frameworks. Looking forward, bank supervisors point to scope for further improving risk management and central banks must also remain alert to evolving system-wide risks.

Specifically concerning capital market activities, the report's executive summary states that "Crisis-era losses combined with regulatory changes have motivated a significant reduction in risk and scale in the non-equity trading and market-making businesses of a number of global banks"; and goes on to state: "The withdrawal of some banks from capital markets-related business has coincided with signs of fragile liquidity in some markets, although causality remains an open question."

This aspect is elaborated on in section 5.2 of the report, *Banks' Role in Facilitating Capital Market Activity*, which includes "a particular focus on non-equity trading businesses, which have experienced considerable adjustment as a result of tighter regulation and the unwinding of pre-crisis excesses." Among other things, it is stated that the topic of market liquidity "is still an area of active debate among academics, regulators and market participant" and that "more research is needed on the link between fixed income liquidity and the real economy." The subsequent *Key Messages*, in section 6 of the report, include a related paragraph starting with the highlighted statement that "Some banks have retreated from capital market-related business."

Among other points in the report's executive summary, it is stated that "consolidation and preservation of gains in bank resilience requires ongoing surveillance, risk management and a systemic perspective", allied to which "authorities should monitor the ongoing adaptation and evolution in the nature and locus of risk-taking within the banking sector and the financial system more broadly" and "In this regard, the group sees scope for the international supervisory community to undertake a post-crisis study of bank risk management practices."

Also, among the subsequent *Key Messages*, in section 6 of the report, it is highlighted that "The evolving nature of systemic risk requires surveillance, particularly on certain key areas." Points associated with this include that "The shifting of some risk out of the banking sector after the crisis highlights the need for continuing central bank investment in systemic risk analysis of the non-bank financial sector. This includes, for example, the monitoring of CCPs' resilience, liquidity risks associated with the growing size of portfolios of asset managers, and the activities of shadow banks in providing intermediation services."

On 25 January, EIOPA published its *Risk Dashboard* based on the third-quarter 2017 data. The results show that the risk exposure of the insurance sector in the EU remained overall stable. Despite positive macro and market trends, the risks linked to the low interest rates and to potential credit risk mispricing continued to be major concerns.

Market perception remained stable with some improvements in the rating outlooks. The data covered by this Risk Dashboard is based on financial stability and prudential reporting of a sample of 97 insurance groups and 2,963 solo insurance undertakings.

On 31 January, the EBA launched its 2018 EU-wide stress test and released the macroeconomic scenarios. The adverse scenario implies a deviation of EU GDP from its baseline level by 8.3% in 2020, resulting in the most severe scenario to date. The EBA expects to publish the results of the exercise by 2 November. In conjunction with this, the ESRB published details regarding the adverse scenario for the test.

Alongside this, also on 31 January, the ECB announced that it will examine 37 euro area banks as part of the 2018 EU-wide stress test conducted with the EBA. In line with the EBA's selection criteria, these banks, which are directly supervised by the ECB, represent 70% of total euro area banking assets. The EBA will coordinate the EU-wide exercise, in cooperation with the ECB and national authorities; and the test will be conducted according to the EBA's methodology, templates and scenarios.

The four Greek banks directly supervised by the ECB will undergo the same stress test under the EBA scenario and methodology, but their results will be made available sooner; and the ECB will conduct its own stress test, in parallel, for those significant institutions not covered by the EU-wide EBA stress test.

On 6 February, EIOPA published the first in a series of papers with the aim of contributing to the debate on systemic risk and macroprudential policy. Until now, the debate has mainly focused on the banking sector, but through this series of papers EIOPA aims to ensure that any further extension of the debate to the insurance sector fully reflects the industry's specific nature.

This first paper outlines the lessons learnt from the financial crisis and the banking sector affecting the insurance sector, as well as the current status of debate within the sector. It identifies and analyses the sources of systemic risk in insurance outlining three potential sources: entity-based, activity-based and behaviour-based. The paper also includes a proposal for a macroprudential framework for insurance and defines specific operational objectives based on the previously-identified sources of systemic risk.

Published on 16 February, *Business Cycles and the Balance Sheets of the Financial and Non-financial Sectors* is an ESRB working paper. The author proposes and estimates a dynamic model of financial intermediation to study the different roles of the condition of banks' and firms' balance sheets in real activity.

The net worth of firms determines their borrowing capacity both from households and banks. Banks provide risky loans to multiple firms and use their diversified portfolio as collateral to borrow from households. This intermediation process allows additional funds to flow from households to firms. Banks require net worth for intermediation as they are exposed to aggregate risk. The author finds that this newly modelled mechanism accounts for 40% of the fall in output and 80% of the fall in bank net worth during the Great Recession. And, the model is consistent with the different dynamics of the share of bank loans in total firm debt and credit spreads during the recessions of 1990, 2001, and 2008.

Published on 23 February, *Rethinking Financial Stability* is a Bank of England staff research paper. The authors provide an overview of the state of progress of post-crisis international regulatory reforms and assess whether they have achieved their objectives and where gaps remain. They find that additional insights gained since the start of the reforms paint an ambiguous picture on whether the current level of bank capital should be higher or lower.

Additionally, they present new evidence that a combination of different regulatory metrics can achieve better outcomes in terms of financial stability than reliance on individual constraints in isolation. They discuss in depth several recurring themes of the regulatory framework, such as the appropriate degree of discretion versus rules, the setting of macroprudential objectives, and the choice of policy instruments. And, they conclude with suggestions for future research and policy.

Additional insights gained since the start of the reforms paint an ambiguous picture on whether the current level of bank capital should be higher or lower.

On 27 February, the ESRB published its analysis of the use of structural buffers – ie the buffer for global systemically important institutions (G-SIIs), the buffer for other systemically important institutions (O-SIIs) and the systemic risk buffer (SRB) – in the EU over the last three years. The entry into force of CRD IV and CRR on 1 January 2014 provided Member States with a harmonised set of instruments to address both cyclical and structural systemic risks at national level; and the Flagship Report and the first issue of the ESRB Handbook, both published in 2014, provided initial guidance on the use of these instruments.

Since their publication, more practical experience with structural buffers has been gained – with all Member States having implemented frameworks for identifying O-SIIs and setting buffer rates, while several Member States have also activated the SRB for different systemic risks. Based on current experience with structural buffers and on economic analysis, additional guidance for national authorities has been included in the revised ESRB Handbook.

Alongside this, the ESRB published an opinion on how the EU legal framework for structural buffers could be enhanced in order to apply the macroprudential toolkit more effectively, thereby strengthening macroprudential policy and protecting the Single Market. The main proposals, which should not be understood as formal ESRB warnings or recommendations, include:

- a substantial increase in the O-SII cap from 2% to 3% with the possibility for designated authorities to impose buffers higher than 3%, subject to approval from the European Commission;
- a substantial increase in the additional O-SII buffer cap on subsidiaries: the O-SII buffer for subsidiaries of EU parent institutions should not exceed the fully phased-in O-SII or G-SII buffer applicable to the group at consolidated level by more than 2 percentage points;
- an upgrade of the SRB to the status of a dedicated instrument targeting structural systemic risk – this would require the possibility of a sectoral application of the instrument and of multiple SRB applications, to allow authorities to address distinct specific risk;
- delineation of the SRB and O-SII buffer; structural buffers should be additive in so far as they target different systemic risks; and
- simplification and clarification of the processes and improvements in transparency.

On 5 March, the FSB published the *Global Shadow Banking Monitoring Report 2017*, which presents the results of its seventh annual monitoring exercise to assess global trends and risks from shadow banking activities. The 2017 monitoring exercise covers data up to end-2016 from 29 jurisdictions, which together represent over 80% of global GDP, including, for the first time, Luxembourg. Also, for the first time, the report assesses the involvement of non-bank financial entities in China in credit intermediation that may pose financial stability risks from shadow banking, such as maturity/liquidity mismatches and leverage.

The main findings are:

- The activity-based, narrow measure of shadow banking grew by 7.6% in 2016 to $45.2 trillion for the 29 jurisdictions, representing 13% of total financial system assets of these jurisdictions.
- CIVs with features that make them susceptible to runs (eg open-ended fixed income funds, credit hedge funds and MMFs), which represent 72% of the narrow measure, grew by 11% in 2016. The considerable trend growth of these CIVs – 13% on average over the past five years – has been accompanied by a relatively high degree of investment in credit products and some liquidity and maturity transformation, highlighting the importance of implementing the, January 2017, FSB *Policy Recommendations on Structural Vulnerabilities from Asset Management Activities*.
- Assets of market intermediaries that depend on short-term funding or secured funding of client assets (eg broker-dealers) declined by 3%, with these intermediaries accounting for 8% of the narrow measure by end-2016. Reflecting their business models, broker-dealers in some jurisdictions employ significant leverage, although it is lower than the levels prior to the 2007-09 global financial crisis.
- Assets of non-bank financial entities engaged in loan provision that is dependent on short-term funding, such as finance companies, shrank by almost 4% in 2016, to 6% of the narrow measure. In some jurisdictions, finance companies tend to have relatively high leverage and maturity transformation, which increases their susceptibility to roll-over risk during period of market stress.
- In 2016, the wider "Other Financial Intermediaries" (OFIs) aggregate, which includes all financial institutions that are not central banks, banks, insurance corporations, pension funds, public financial institutions or financial auxiliaries, grew by 8% to $99 trillion in 21 jurisdictions and the euro area, faster than banks, insurance corporations and pension funds. OFI assets now represent 30% of total financial assets, the highest level since at least 2002.
- The 2017 monitoring exercise also benefited from improved data submissions by authorities to measure interconnectedness among financial sectors and to assess short-term wholesale funding trends,

including repos. On an aggregated basis, both banks' credit exposures to, and funding from, OFIs have continued to decline in 2016, and are at 2003-06 levels.

In relation to enhancing system-wide monitoring and dampening pro-cyclicality and other financial stability risks associated with SFTs, the FSB has approved in October 2017 the operational arrangements to initiate data collection and aggregation of global SFTs, beginning with end-2018 data. *Reporting Guidelines* for this data collection were published alongside this latest monitoring report.

On 6 March, the BCBS published the results of its latest Basel III monitoring exercise based on data as of 30 June 2017. The BCBS's finalisation of the Basel III reforms is not yet reflected in the results, as the collection of relevant data for those reforms started for the end-2017 reporting date. It is reported that all banks meet Basel III minimum and target CET1 capital requirements as agreed up to end-2015; and all G-SIBs meet both fully phased-in liquidity requirements. Data have been provided for a total of 193 banks – this comprises 106 large internationally active "Group 1 banks", with Tier 1 capital of > €3 billion (including all 30 banks that have been designated as G-SIBs; and 87 "Group 2 banks" (ie banks that have Tier 1 capital of < €3 billion or are not internationally active).

Alongside this, also on 6 March, the EBA published its thirteenth report of the CRDIV-CRR/Basel III monitoring exercise on the European banking system. This exercise presents aggregate data on EU banks' capital, leverage, and liquidity ratios assuming full implementation of the CRD IV-CRR/Basel III framework. Overall, the results, based on data as of 30 June 2017, show a further improvement of European banks' capital positions, with a total average CET1 ratio of 13.8% (13.4% as of 31 December 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.

Across major markets, spreads between corporate and sovereign bond yields remain compressed, particularly for high-yield corporate bonds.

Published on 9 March, *Macroprudential Stress Tests: A Reduced-Form Approach to Quantifying Systemic Risk Losses* is an IMF staff working paper. The authors present a novel approach that incorporates individual entity stress testing and losses from systemic risk effects (SE losses) into macroprudential stress testing. SE losses are measured using a reduced-form model to value financial entity assets, conditional on macroeconomic stress and the distress of other entities in the system. Under the authors' approach, SE losses capture the effects of interconnectedness structures that are consistent with markets' perceptions of risk. They then show how SE losses can be decomposed into the likelihood of distress and the magnitude of losses, thereby quantifying the contribution of specific entities to systemic contagion. To illustrate the approach, they quantify SE losses due to Lehman Brothers' default.

A statement from its meeting, on 12 March, reveals that the Bank of England's Financial Policy Committee (FPC) reviewed the outlook for UK financial stability, risks to UK financial stability from Brexit, and risks from crypto-assets (which the FPC judges do not currently pose a material risk to UK financial stability). The FPC also finalised the main elements of the design of the 2018 stress test of major UK banks, which will be the same as that used in 2017 and is, therefore, more severe than the global financial crisis.

The FPC continues to judge that, apart from those related to Brexit (which could result in more severe conditions than in the stress test and disrupt the financial system), domestic risks remain standard overall, and that risks from global vulnerabilities remain material. While the outlook for global growth has strengthened further, there are material risks associated with interest rate volatility. The principal risks are in debt markets. Across major markets, spreads between corporate and sovereign bond yields remain compressed, particularly for high-yield corporate bonds.

On 20 March, ESMA published its latest *Trends, Risks, and Vulnerabilities (TRV) Report* (No 1, 2018), stating that European securities markets, infrastructures and investors remain at risk. This TRV, which covers the second half of 2017, finds that overall risk levels for the EU's securities

markets remained stable but at high levels for most risk categories. However, February 2018 saw severe market corrections and the return of equity market volatility, confirming ESMA's prevailing concerns. On the other hand, the level of credit risk eased, from very high to high, reflecting a strengthening macroeconomic environment and higher credit ratings in several EU Member States.

The TRV identifies the following key risks in EU securities markets:

- market risk remains at very high level due to concerns about high asset market valuations and prevailing geopolitical uncertainties, such as around the current Brexit negotiations;
- credit risk has eased in relation to an improving macroeconomic environment but remains high due to possible and sudden repricing in risk premia;
- operational risk continued to be elevated with a deteriorating outlook, with extensive concerns around cyber security; and
- retail investor risks associated with investments in virtual currencies and ICOs.

On 21 March, EIOPA published the second in its series of papers with the aim of contributing to the debate on systemic risk and macroprudential policy. This second paper identifies, classifies and provides a preliminary assessment of the tools or measures already existing within the Solvency II framework, which could mitigate any of the systemic risk sources that were identified in the EIOPA's first paper *Systemic Risk and Macroprudential Policy in Insurance* published in February. The paper also includes a detained annex on the macroprudential impact of some of the long-term guarantees measures under stress.

The General Board of the ESRB held its 29th regular meeting, on 22 March. The General Board noted that stronger and more broad-based economic growth has improved the risk outlook for the stability of the EU financial system. However, tail risks remain elevated amid significant political, geopolitical and policy uncertainties. The General Board exchanged views on the major trends in macroprudential policy in the EU in 2017 and noted that the ESRB will publish its *Review of Macroprudential Policy in the EU in 2017* in Q2 2018. The General Board also discussed the adverse scenario prepared jointly by ECB staff and the ESRB Task Force on Stress Testing for the 2018 EU-wide insurance stress test by EIOPA.

Allied to this, the ESRB subsequently published its latest quarterly *Risk Dashboard*. Overall, market-based indicators of systemic stress in the EU showed an increase over the past quarter. From a macro risk perspective, economic recovery in the EU continued in the 4Q 2017, but debt levels remain elevated across countries and sectors in the EU. Banking sector resilience continued to strengthen in 4Q 2017, with bank profitability in the EU continuing to improve. Solvency and profitability indicators still suggest that the EU insurance sector is performing well, and no big shifts have been observed in insurers' asset allocation over the last four quarters. The total assets of investment funds, OFIs, insurance corporations and pension funds increased more during the 3Q 2017 than the total assets held by credit institutions.

Published on 28 March, *Towards a Sectoral Application of the Countercyclical Capital Buffer (CCyB): A Literature Review* is a BCBS staff working paper. Overall, the authors consider that this review shows that there is a justified need for sectoral macroprudential tools, and that a sectoral CCyB may be a useful complement to both the Basel III CCyB and existing targeted instruments in the macroprudential toolkit. Yet, CCyBs, both broad-based and sectoral, remain largely untested and more empirical work is needed to assess their ability to achieve the different objectives that may be attributed to them. Furthermore, a sectoral application of the CCyB entails several operational challenges, such as defining modalities on when to activate a sectoral CCyB and on its interactions with the Basel III CCyB as well as with other (targeted) instruments, which adds to complexity.

Published on 29 March, *Firms' Credit Risk and the Onshore Transmission of the Global Financial Cycle* is a BIS staff working paper, in which the authors investigate the role of firms' credit risk in the onshore transmission of international bond market conditions. They show that reductions in the global price of risk, measured by the excess bond premium, encourage more international bond borrowing by smaller and younger firms. Due to informational asymmetries, these firms pay a higher credit spread – thus their funding costs, and consequently their international borrowing, are more tightly linked to the global price of risk. The funds borrowed in response to favourable market conditions cause their balance sheets to deteriorate – over a three-year horizon, leverage increases, in support of capital expenditure, and cash holdings increase.

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ICMA Capital Market Research

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

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

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

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

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

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

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

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

Join us at the 50th annual ICMA conference in Madrid a perfect opportunity to meet old friends and make new ones with delegates coming from bond markets around the world. ICMA member firms have an allocation of free places and the conference is also open to all interested financial market participants and press.

Contact: membership@icmagroup.org

WEDNESDAY MAY 30, 2018

20.30 - 23.30 **Welcome Reception,** Museo Nacional del Prado

Welcome remarks Baron Íñigo Méndez de Vigo y Montojo, Minister of Education, Culture and Sport, Spain

THURSDAY MAY 31, 2018

ICMA Annual General Meeting & Conference, Meliá Castilla Hotel

08.00 **Registration and Exhibition open**

09.00 **Annual General Meeting (ICMA members only)**

11.30 **Lunch**

13.00 **Open of Conference**

13.00 **Welcome remarks**
Chairman, ICMA

13.05 **Opening keynote address**

13.20 **Keynote address: Javier Alonso,** Deputy Governor, Banco de España

13.35 **Keynote address: José Manuel González-Páramo,** Executive Board Director, Head of Global Economics, Regulation and Public Affairs, Banco Bilbao Vizcaya Argentaria

13.50 **Panel: Forum of business leaders on global financial market strategy**

Panellists:
Cyrus Ardalan, Chairman, Citi Global Markets Ltd
Samir Assaf, Group Managing Director and Chief Executive Officer, Global Banking and Markets, HSBC Holdings plc
Nils Bolmstrand, Chief Executive Officer, Nordea Asset Management
Piyush Gupta, Chief Executive, DBS Group
Rana Kapoor, Managing Director & CEO, YES BANK
Sylvie Matherat, Chief Regulatory Officer and Member of Management Board, Deutsche Bank AG

14.50 **Coffee break**

15.20 **Keynote address: José Antonio Alvarez,** Chief Executive Officer, Santander Group

15.35 **Keynote address: Valdis Dombrovskis,** Vice President, European Commission

15.55 **Keynote address: Steven Maijoor,** Chair, European Securities and Markets Authority

16.05 **Panel: The international capital market: Challenges & opportunities**
Moderator: **Martin Egan,** Vice Chairman of the Global Markets Client Board, BNP Paribas

Panellists:
Thijs Aaten, Managing Director Treasury & Trading, APG Asset Management
Juan Blasco, Global Head of Syndicate, BBVA
Andy Cairns, Senior Managing Director, Head of Global Corporate Finance, First Abu Dhabi Bank
Sir Robert Stheeman, Chief Executive Officer, UK Debt Management Office
Pierre van Peteghem, Treasurer, Asian Development Bank

16.55 **Panel: International benchmark reform**
Moderator: **Paul Richards,** Managing Director, Head of Market Practice and Regulatory Policy, ICMA

Panellists:
Roman Baumann, Head of Money Market, Swiss National Bank
David Bowman, Advisor, Board of Governors, The Federal Reserve
Cornelia Holthausen, Deputy Director General, European Central Bank
Edward Ocampo, Senior Advisor - Markets, Bank of England
Edwin Schooling Latter, Head of Markets Policy, Strategy & Competition, Financial Conduct Authority

17.40 **Closing keynote: Arunma Oteh,** Vice President and Treasurer, World Bank

17.55 **Closing remarks** **Martin Scheck,** Chief Executive, ICMA

18.00 **Close**

20.00 - 01.00 **Gala Reception, CentroCentro Palacio de Cibeles**

FRIDAY JUNE 1, 2018

08.30 **Exhibition open**

09.30 **Opening remarks** **Martin Scheck,** Chief Executive, ICMA

09.35 **Keynote address: Barbara Novick,** Vice Chairman, BlackRock

09.50 **Panel: Challenges in a changing asset management industry**
Moderator: **Robert Parker,** Chairman, ICMA Asset Management and Investors Council
Panellists:
Ibrahima Kobar, Deputy Chief Executive Officer and Global Chief Investment Officer, Ostrum Asset Management
Ingo Mainert, Managing Director and Chief Investment Officer, Multi Asset Europe, Allianz Global Investors
Sheila Patel, Chief Executive Officer, International Goldman Sachs Asset Management
Han Rijken, Global Head of Credit and Member of the Global Investment Leadership Team, NN Investment Partners

10.50 **Coffee break**

11.20 **Keynote address: Ashley Alder,** Chairman of the Board, International Organization of Securities Commissions

11.35 **Panel: Secondary bond markets: a rapidly transforming landscape**
Panellists:
The Viscount Bridport, Senior Managing Partner and Founder, bridport & co
Joseph Pinto, Global Chief Operating Officer, AXA Investment Managers
Christophe Roupie, Head of Europe and Asia, MarketAxess
Zoeb Sachee, Head of Euro Government and SSA Trading, Citi
Torsti Silvonen, Deputy Director General, DG-Market Operations, European Central Bank

12.35 **Keynote address: Margaret L. Kuhlow,** Finance Practice Leader, WWF International

12.50 **Panel: Developments in green, social and sustainability finance**
Moderator: **Ashley Schulten,** Managing Director, Head of Responsible Investment, Global Fixed Income, BlackRock
Panellists:
Suzanne Buchta, Managing Director, Global Head of ESG Fixed Income, Bank of America Merrill Lynch
Bertrand de Mazières, Director General Finance, European Investment Bank
Fernando Navarrete, Chief Financial Officer, Instituto De Crédito Oficial
Dr. R. Seetharaman, Chief Executive Officer, Doha Bank
Yu Sun, Chief Executive Officer and General Manager, Bank of China Limited, London Branch

13.50 **Keynote address**

14.05 **Closing remarks** **Martin Scheck,** Chief Executive, ICMA

14.15 **Lunch**

15.00 **Close**

GET INVOLVED

We want you to get the maximum value from your firm's membership of the International Capital Market Association (ICMA). To help you to do this we've produced 'Get involved!', a quick guide to what ICMA does and how it works with its members. This has been prepared by the members of the ICMA Future Leaders group, who are all professionals in the early stages of their careers, to provide an insight into the work of the association and the services it offers.

Diary 2018

ICMA Events

25 April *Register*

Social bonds - from niche to mainstream, London, 25 April: The social bond market has quadrupled in issuance volume since the launch of the Social Bond Principles in 2017, with annual issuance increasing from $2.1bn in 2016 to $8.8bn in 2017. As more diverse issuers consider coming to the market, what can be done to encourage growth of the product? Issuers, investors, underwriters and infrastructure providers will address this question at the seminar.

3 May *Register*

Embracing change: future proofing your career with FinTech, London, 3 May: In the future, most employment will be subject to technologically-driven change, so embracing flexibility and adaptability will be key as we reinvent ourselves throughout our working lives. Start now, by registering for this IWN event which sets out to illuminate the world of FinTech, with a panel of female FinTech experts sharing their own career experiences and knowledge. The event is open to all ICMA members (male or female) and is followed by a session of structured networking.

14 June *Register*

2018 Green and Social Bond Principles Annual General Meeting & Conference, Hong Kong, 14 June: The GBP and SBP AGM & conference will be held for the first time in Asia, signifying the growing influence of Asia in the development of green bonds in particular, and sustainable finance more widely, as well as recognising Hong Kong's status and importance as an international financial centre. It is co-organised by the International Capital Market Association (ICMA) and the Hong Kong Monetary Authority (HKMA) and supported by the Hong Kong Financial Services Development Council (FSDC).

27 June *Register*

The ICMA CBIC & The Covered Bond Report Conference, Frankfurt, 27 June: 2018 is a landmark year for the covered bond market with the European Commission announcing a planned Directive in March. Action on SME covered bonds is also likely, while the ECB manages the gradual easing of CBPP3, and market participants push ahead with green covered bonds. These topics will be explored, with a focus on the buy-side's perspective, at the eighth annual Covered Bond Investor Conference, hosted by the ICMA Covered Bond Investor Council and The Covered Bond Report.

ICMA Workshops

14 June *Register*

European Regulation: An Introduction for Capital Market Practitioners, London, 14 June: How much do you know about the new regulations that are already in force and impacting your daily work in the capital market and the ones that are still in the pipeline? How do the institutions of Europe work together to develop new regulation? ICMA's one-day, fast-track course on European regulation for capital market practitioners gives an overview of the new regulatory landscape for financial institutions in Europe.

21 June *Register*

Bond syndication practices for compliance professionals and middle office professionals, London, 21 June: 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. It explains precisely how the deal is done, starting with first steps in the pre-launch process - looking at the pitch book, the mandate, the roadshow and the prospectus - through syndication, including book building and allocation, up to and including the final public launch of the issue.

27-29 June *Register*

Repo and securities lending under the GMRA and GMSLA, London, 27-29 June: Analyses how repo and securities lending transactions operate within the framework provided by the Global Master Repurchase Agreement (GMRA) and the Global Master Securities Lending Agreement (GMSLA), and highlights the issues that need to be addressed by users. These two separate but increasingly overlapping master agreements are the essential underpinnings of the cross-border repo and securities lending markets.

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

Courses 2018

ICMA EE in numbers

Over 6,000 people now have the ICMA Fixed Income Certificate (FIC) qualification on their CVs – the programme ran for the first time in 1977.

984 delegates attended our courses in 2017 – that's an ICMA EE record – and they came from all over the world, 51 countries in total.

We also ran 31 in-house programmes last year, across four continents.

We had good practical exercises. It's always worth attending ICMA's courses!

New in 2018

Specialist Programme – OTC Derivatives Operations: Products, Collateral and EMIR

Derivatives are widely used to insure against risk in financial markets, with many types of derivative products being traded and settled directly on an Over-the-Counter (OTC) basis.

ICMA Executive Education has developed a new Specialist Programme focused on how trades and collateral are processed under the new EMIR Regulation. The course focuses on the relationship between the various components, the risks at each step and the mitigating controls.

Skills to be gained from this programme:

- Expert knowledge of OTC derivatives products and the specific sequential steps in their processing, including the principles of collateral and its management
- A full grasp of the background of EMIR, trade reporting to trade repositories and the principles of centrally and non-centrally cleared trades
- Efficient operational processing by both buy-side and sell-side firms
- A thorough understanding of the most important existing and new aspects of OTC derivatives operations

The course begins at an elementary level, but then multiple challenging concepts are introduced, covering trades executed with bilateral counterparties and central counterparties.

Details of the next course

London, 25-26 June
Cost: £1,650 for members and £1,950 for non-members
Register now

Specialist programmes

In addition to our examined qualifications, ICMA Executive Education offers non-examined specialist programmes throughout the year. These courses are 1-2 days in length and are focused on a single topic giving you an opportunity to network and discuss the issues affecting the financial markets with your industry peers.

Sign up now for these specialist programmes from ICMA Executive Education

Fixed Income Portfolio Management
London: **3-4 May 2018**
Corporate Actions – An Introduction
London: **22-23 May 2018**
Corporate Actions – Operational Challenges
London: **24-25 May 2018**
Credit Default Swaps – Pricing, Applications and Features
London: **30-31 May 2018**
Compliance in Fixed Income
London: **5 June 2018**
Securities Lending & Borrowing
London: **18-19 June 2018**

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

GLOSSARY

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
AMI-SeCo	Advisory Group on Market Infrastructure for Securities and Collateral
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
BMR	EU Benchmarks Regulation
bp	Basis points
BRRD	Bank Recovery and Resolution Directive
CAC	Collective action clause
CBIC	ICMA Covered Bond Investor Council
CCBM2	Collateral Central Bank Management
CCP	Central counterparty
CDS	Credit default swap
CFTC	US Commodity Futures Trading Commission
CGFS	Committee on the Global Financial System
CICF	Collateral Initiatives Coordination Forum
CIF	ICMA Corporate Issuer Forum
CMU	Capital Markets Union
CNAV	Constant net asset value
CoCo	Contingent convertible
COP21	Paris Climate Conference
COREPER	Committee of Permanent Representatives (in the EU)
CPMI	Committee on Payments and Market Infrastructures
CPSS	Committee on Payments and Settlement Systems
CRA	Credit Rating Agency
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CSD	Central Securities Depository
CSDR	Central Securities Depositories Regulation
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
ESM	European Stability Mechanism
ESMA	European Securities and Markets Authority
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
FRTB	Fundamental Review of the Trading Book
FSB	Financial Stability Board
FSC	Financial Services Committee (of the EU)
FSOC	Financial Stability Oversight Council (of the US)
FTT	Financial Transaction Tax
G20	Group of Twenty
GBP	Green Bond Principles
GDP	Gross Domestic Product
GHOS	Group of Central Bank Governors and Heads of Supervision
GMRA	Global Master Repurchase Agreement
G-SIBs	Global systemically important banks
G-SIFIs	Global systemically important financial institutions
G-SIIs	Global systemically important insurers
HFT	High frequency trading
HMRC	HM Revenue and Customs
HMT	HM Treasury
HQLA	High Quality Liquid Assets
HY	High yield
IAIS	International Association of Insurance Supervisors
IASB	International Accounting Standards Board
IBA	ICE Benchmark Administration
ICMA	International Capital Market Association
ICSA	International Council of Securities Associations
ICSDs	International Central Securities Depositaries
IFRS	International Financial Reporting Standards
IG	Investment grade
IIF	Institute of International Finance
IMMFA	International Money Market Funds Association
IMF	International Monetary Fund
IMFC	International Monetary and Financial Committee
IOSCO	International Organization of Securities Commissions
IRS	Interest rate swap
ISDA	International Swaps and Derivatives Association
ISLA	International Securities Lending Association
ITS	Implementing Technical Standards
KfW	Kreditanstalt 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
MAR	Market Abuse Regulation
MEP	Member of the European Parliament
MiFID	Markets in Financial Instruments Directive
MiFID II	Revision of MiFID (including MiFIR)
MiFIR	Markets in Financial Instruments Regulation
MMCG	ECB Money Market Contact Group
MMF	Money market fund
MOU	Memorandum of Understanding
MREL	Minimum requirement for own funds and eligible liabilities
MTF	Multilateral Trading Facility
NAFMII	National Association of Financial Market Institutional Investors
NAV	Net asset value
NCA	National competent authority
NCB	National central bank
NPL	Non-performing loan
NSFR	Net Stable Funding Ratio (or Requirement)
OAM	Officially Appointed Mechanism
OJ	Official Journal of the European Union
OMTs	Outright Monetary Transactions
ORB	London Stock Exchange Order book for Retail Bonds
OTC	Over-the-counter
OTF	Organised Trading Facility
PCS	Prime Collateralised Securities
PMPC	ICMA Primary Market Practices Committee
PRA	UK Prudential Regulation Authority
PRIIPs	Packaged Retail and Insurance-Based Investment Products
PSEs	Public Sector Entities
PSI	Private Sector Involvement
PSIF	Public Sector Issuer Forum
QE	Quantitative easing
QIS	Quantitative impact study
QMV	Qualified majority voting
RFQ	Request for quote
RFRs	Near risk-free rates
RM	Regulated Market
RMB	Chinese renminbi
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 asset
SBBS	Sovereign bond-backed securities
SEC	US Securities and Exchange Commission
SFT	Securities financing transaction
SGP	Stability and Growth Pact
SI	Systematic Internaliser
SLL	Securities Law Legislation
SMEs	Small and medium-sized enterprises
SMPC	ICMA Secondary Market Practices Committee
SMSG	Securities and Markets Stakeholder Group (of ESMA)
SPV	Special purpose vehicle
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SRO	Self-regulatory organisation
SSAs	Sovereigns, supranationals and agencies
SSM	Single Supervisory Mechanism
SSR	EU Short Selling Regulation
STORs	Suspicious transactions and order reports
STS	Simple, transparent and standardised
T+2	Trade date plus two business days
T2S	TARGET2-Securities
TD	EU Transparency Directive
TFEU	Treaty on the Functioning of the European Union
TLAC	Total Loss-Absorbing Capacity
TMA	Trade matching and affirmation
TRs	Trade repositories
UKLA	UK Listing Authority
VNAV	Variable net asset value

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