European Leveraged Finance Association

BRIEFINGS

LEGAL & REGULATORY

8 June 2021

Legal and Regulatory Updates

31/05/2021 – 04/06/2021

Key Highlights

- This Legal & Regulatory Update covers the week commencing **31/05/2021**.
- PRA publishes its Regulatory Digest - May 2021.
- Sterling Risk-Free Rate Working Group publishes its newsletter for May 2021.
- ESMA publishes its first Risk Dashboard (RD) for 2021 covering the first quarter of the year.
- ESMA publishes latest edition of its Newsletter.
- ESRB publishes a second report on macroprudential policy issues arising from the low interest rate environment in the financial system of the European Union.
- European Commission publishes its Banking and Finance Newsletter for May 2021.
- FINMA specifies transparency obligations for climate risks.
- IOSCO issues statement on benchmarks transition.
- FSB issues statements to support a smooth transition away from LIBOR by end 2021.
- In this update, we also cover some of the most important news on leveraged finance published by the Financial Times during the week.

Bank of England (BoE)

31 May – 04 June 2021: Speeches, Letters & Publications

During the week, the Bank of England (BoE) released the following speeches, announcements and other publications that might be of interest to our readers:

- PRA publishes its Regulatory Digest May 2021 – the PRA Regulatory Digest is for people working in the UK financial services industry and highlights key regulatory news and publications delivered for the month
- Sterling Risk-Free Rate Working Group publishes its newsletter for May 2021
- Tackling climate for real: the role of central banks – Speech by Andrew Bailey
- Tackling climate for real: progress and next steps – Speech by Andrew Bailey
- Monthly Decision Maker Panel data May 2021 – the DMP is a survey of Chief Financial Officers from small, medium and large UK businesses. The BoE uses it to monitor developments in the economy and to track businesses' views
- Report: Deep, liquid, and transparent (DLT) assessment of the Sterling Overnight Index Average (SONIA) Overnight Index Swap (OIS) market – this report sets out the results and analysis for the PRA's first DLT assessment of the SONIA OIS market

Financial Reporting Council (FRC)

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the Financial Reporting Council (FRC) released the following speeches, announcements, and publications that might be of interest to our readers:

- FRC Webinar: Review of Interim Reporting – ahead of the 2021 interim reporting season, the FRC invites you to a webinar to learn more about its recent review of interim reporting which highlighted examples of good reporting practice and areas where further improvements are required. High-quality reporting is vital for investors and other users of accounts to make better informed decisions about a company's health and prospects. The webinar will be particularly useful for preparers, auditors, investors and other users of interim reports

European Securities and Markets Authority (ESMA)

03 June 2021: ESMA publishes its first Risk Dashboard (RD) for 2021 covering the first quarter of the year

The European Securities and Markets Authority published its first Risk Dashboard (RD) for 2021 covering the first quarter of the year. According to RD, fixed income valuations are now far above their pre-COVID-19 levels, in part due to continued monetary policy support. A sudden risk reassessment, amid the general decoupling of securities prices from economic fundamentals, remains the main risk for EU financial markets and ESMA therefore maintains its risk assessment. Credit risk is likely to increase further due to increasing corporate and public debt levels. Looking ahead, ESMA anticipates a prolonged period of risk to institutional and retail investors of further – possibly significant – market corrections and sees very high risks across its whole remit. The extent to which these risks will further materialise will critically depend on market expectations on monetary and fiscal policy support as well as on the pace of the economic recovery.

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the ESMA released the following speeches, announcements, and publications that might be of interest to our readers:

- ESMA publishes latest edition of its Newsletter
- ESMA publishes Final Report on the MiFIDII/MiFIR obligations on market data

European Banking Authority (EBA)

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the European Banking Authority (EBA) released the following speeches, announcements, letters and publications that might be of interest to our readers:

- EBA and ESMA publish provisional list of instruments and funds for the smallest investment firms under the Investment Firms Regulation – the list is provisional and intended to provide guidance to investment firms and competent authorities ahead of the application of the IFR requirements, as of 26 June 2021
- EBA publishes its 2020 Annual Report

European Systemic Risk Board (ESRB)

01 June 2021: ESRB publishes a second report on macroprudential policy issues arising from the low interest rate environment in the financial system of the European Union

The European Systemic Risk Board (ESRB) published a second report on macroprudential policy issues arising from the low interest rate environment in the financial system of the European Union (EU). The work behind the report, which was conducted by a joint task force of the ESRB's Advisory Technical Committee, the ESRB's Advisory Scientific Committee and the ECB's Financial Stability Committee, began in late 2019 and built on an earlier report that the ESRB published in 2016. The latest analysis has a forward-looking medium-term time horizon of five to ten years. While the report acknowledges cross-country heterogeneity, its focus is predominantly on the EU financial system as a whole and on interest rates in the EU.

The report begins with an extensive analysis of how the low interest rate environment has been driven mainly by structural factors, including demographics, productivity, excess savings and low investment. Looking beyond recent cyclical developments, the coronavirus (COVID-19) shock may have increased the likelihood and persistence of a "low for long" scenario, making it "even lower for even longer".

The risk analysis of the report identifies four areas of concern owing to the low interest rate environment:

- profitability and resilience of banks, as the negative effects of existing structural problems in the EU banking sector, including overcapacity and cost inefficiencies, are being compounded;
- indebtedness and viability of borrowers, who are taking on more debt as a result of their search for yield;
- systemic liquidity risk, as the financial system has become more sensitive to market shocks, also as a result of structural changes;
- sustainability of the business models of insurers and pension funds offering longer-term return guarantees, as they are coming under increasing pressure.

Furthermore, the report identifies key actions to complete the policy framework outlined in 2016, in the following areas: (i) sustainability of the business models of insurance companies and pension funds offering longer-term return guarantees; (ii) implementation and monitoring of lending standards across the financial system; (iii) monitoring of leverage in the financial system; (iv) analysis of interconnectedness; (v) identification of regulatory arbitrage; and (vi) subsequent analysis of the need for activity-based regulation.

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the ESRB released the following speeches, announcements, letters and publications that might be of interest to our readers:

- A quantitative analysis of the countercyclical capital buffer – Working Paper Series No 120 / June 2021

European Central Bank (ECB)

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the European Central Bank (ECB) released the following speeches, announcements, letters and publications that might be of interest to our readers:

- Results of the Survey on the Access to Finance of Enterprises (SAFE)
- The embrace of the horizon: Forcefully moving with the changing tide for climate action in financial sector policies – Speech by Frank Elderson, Chair of the Central Banks and Supervisors Network for Greening the Financial System, Member of the Executive Board and Vice-Chair of the Supervisory Board of the ECB, at The Green Swan Conference Coordinating finance on climate
- The embrace of the horizon: Forcefully moving with the changing tide for climate action in financial sector policies – Speech by Frank Elderson, Chair of the Central Banks and Supervisors Network for Greening the Financial System, Member of the Executive Board and Vice-Chair of the Supervisory Board of the ECB, at The Green Swan Conference Coordinating finance on climate
- Learning the right lessons from the past – Speech by Christine Lagarde, President of the ECB, on the importance of financial regulation
- The Covid pandemic in the market: infected, immune and cured bonds – Working Paper Series
- Euro area sovereign bond risk premia during the Covid-19 pandemic – Working Paper Series
- The risk management approach to macro-prudential policy – Working Paper Series
- Combining negative rates, forward guidance and asset purchases: identification and impacts of the ECB's unconventional policies – Working Paper Series
- Point targets, tolerance bands, or target ranges? Inflation target types and the anchoring of inflation expectations – Working Paper Series

European Commission

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the European Commission released the following speeches, announcements, letters and publications that might be of interest to our readers:

- European Commission publishes its Banking and Finance Newsletter for May 2021
- Speech by President von der Leyen at the EU Green Week 2021 conference

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Central Bank of Ireland (CBI)

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the Central Bank of Ireland (CBI) released the following speeches, announcements and publications that might be of interest to our readers:

- Central Bank publishes Annual Report & Annual Performance Statement for 2020 – the report highlights the scale and variety of the work undertaken by the Central Bank in 2020

Autorité des marchés financiers (AMF)

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the Autorité des marchés financiers (AMF) released the following speeches, announcements and publications that might be of interest to our readers:

- Sustainability and digitalisation – Speech by Robert Ophèle, AMF Chairman

Swiss Financial Market Supervisory Authority (FINMA)

31 May 2021: FINMA specifies transparency obligations for climate risks

The Swiss Financial Market Supervisory Authority (FINMA) issued a press release to clarify its supervisory practice in the area of disclosure of climate-related financial risks. In doing so it is fulfilling its strategic goal of contributing to the sustainable development of the Swiss financial centre. Besides the consideration of climate risks in supervisory activities and preventing the public from being misled about a product's sustainable characteristics (greenwashing), promoting transparency is FINMA's major focus in this realm.

According to FINMA, banks and insurance companies are required to inform the public adequately about their risks. These also include the consequences of climate change, which could pose significant financial risks for financial institutions in the longer term. FINMA is requiring large banks and insurance companies to provide qualitative and quantitative information in this area and is amending its circulars on disclosure.

International Organization of Securities Commissions (IOSCO)

02 June 2021: IOSCO issues statement on benchmarks transition

The International Organization of Securities Commissions (IOSCO) issued a statement reiterating the importance of ensuring a smooth and timely transition away from LIBOR. In the statement, IOSCO emphasises that the transition away from LIBOR remains a significant regulatory priority. This transition will require market participants to take steps to stop issuance of new products linked to LIBOR and efforts to transition away from LIBOR in legacy contracts that span multiple markets and jurisdictions. For this purpose, the use of LIBOR rates in new contracts should be ceased as soon as practicable and no later than the timelines set out by home authorities and/or national working groups in the relevant currencies.

In light of the significant use of USD LIBOR globally, including in more than one hundred emerging markets and across a wide range of products and financing purposes, IOSCO is cognizant of the importance of reinforcing the transition message and timeline on a global scale. Therefore, IOSCO encourages all global market participants to discontinue new use of USD LIBOR-linked contracts, as soon as practicable and no later than end-2021, to avoid the safety and soundness risks associated with the continued use. In line with its communication and outreach program launched in 2019, IOSCO will continue its efforts to inform relevant stakeholders regarding transition from LIBOR to alternative rates that comply with the IOSCO Principles on Financial Benchmarks.

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the IOSCO released the following speeches, announcements and publications that might be of interest to our readers:

- Monitoring Group Reports on Progress to Implement Recommendations to Strengthen the International Audit and Ethics Standard-Setting System – having completed the development of the transition plan, many aspects of implementation have already begun. Currently, the MG is focusing on the appropriate sequencing of activities to implement the recommendations and on establishing a sustainable funding model. The MG is committed to transparency as the reforms are implemented, and expects to issue further communications as various implementation activities occur

International Capital Market Association (ICMA)

31 May – 04 June 2021: Speeches, Letters & Other Publications

During the week, the International Capital Market Association (ICMA) released the following speeches, announcements and publications that might be of interest to our readers:

- ICMA virtual event: Transition to risk free rates: an official sector panel discussion – ICMA's Paul Richards leads a panel discussion with speakers from the UK Financial Conduct Authority, the Federal Reserve Bank of New York, the Swiss National Bank and the European Central Bank about progress and the remaining challenges in the transition from LIBOR/IBORs to risk-free rates, international coordination, and key messages from the official sector for market firms in the run-up to the end of 2021
- Podcast: Euronext in the European fixed income space – Chris Topple, Euronext CEO, talks to ICMA's Martin Scheck about changes in European fixed income markets post MiFID II and how Euronext has scaled up its fixed income capabilities through recent acquisitions including Borsa Italiana to meet market structure challenges. They discuss the electronification of fixed income markets, the future of fixed income trading and improving post trade efficiency
- Podcast: Asia international bond markets, a conversation with Christophe Roupie of MarketAxess – Andy Hill, Global Head of Secondary Markets at ICMA, speaks with Christophe Roupie, Head of EMEA and APAC at MarketAxess, about recent and ongoing developments in the Asia international bond markets. Christophe shares his observations and insights on a number of aspects, including the internationalization of local markets, the growing predominance of China, the rapid adoption of e-trading and automation across the region, as well as the potential for further transformation of market structure in the near future

Financial Stability Board (FSB)

02 June 2021: FSB issues statements to support a smooth transition away from LIBOR by end 2021

The Financial Stability Board (FSB) published a set of documents to support a smooth transition away from LIBOR by the end of 2021. On 5 March 2021, ICE Benchmark Administration (IBA) and the UK Financial Conduct Authority (FCA) formally confirmed the dates that panel bank submissions for all LIBOR settings will cease, after which representative LIBOR rates will no longer be available. The majority of LIBOR panels will cease at the end of this year, although a number of key US dollar (USD) settings will continue until end-June 2023, to support the rundown of legacy contracts only.

In light of these developments, and to facilitate an orderly transition by end-2021, the FSB has published the following statements and reports that set out recommendations for financial and non-financial sector firms, as well as the authorities, to consider:

- An updated global transition roadmap that, drawing on national working group recommendations, summarises the high-level steps firms will need to take now and over the course of 2021 to complete their transition.
- A paper reviewing overnight risk-free rates and term rates, building on the concept that the tools necessary to complete the transition are currently available. The FSB cautions market participants against waiting for the development of additional tools, in particular forward-looking term risk-free rates.
- A statement on the use of the ISDA spread adjustments in cash products, to support transition particularly in loan markets, which remains an area of concern with much new lending still linked to LIBOR.
- A statement encouraging authorities to set globally consistent expectations that regulated entities should cease the new use of USD LIBOR in line with the relevant timelines for that currency, regardless of where those trades are booked.

The FSB also welcomes the statement on benchmarks transition published by the International Organization of Securities Commissions, which reiterates the importance of ensuring a smooth and timely transition away from LIBOR. Given the limited time available until the end of 2021, the FSB strongly urges market participants to act now to complete the steps set out in its global transition roadmap. The FSB plans to produce its next full report on progress in November 2021.

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In the News

During the week, the Financial Times published the following news that might be of interest to our readers.

Financial Times

- Deal near on forcing companies to disclose climate risks, says central bank chief
  "A global agreement is within reach that would require all listed companies to disclose the risks they face from climate change in a standardised way, the governor of France's central bank has said. François Villeroy de Galhau told the Financial Times that talks between government and central bank officials on new climate risk disclosure rules had progressed faster than expected and that an international framework could be agreed at November's UN COP26 climate conference in the Scottish city of Glasgow"
- The EU's new sustainability rules spell trouble for many businesses
  "Companies and financial institutions need to enhance their capacities on human rights. They need — at a minimum — to develop the skills to conduct due diligence in this area on an ongoing basis; create the governance structures to determine accountability and day-to-day responsibility; and systematically integrate human rights risks in decision-making . . . The Green Deal reflects this realisation. Yet business and finance must play their part by integrating respect for human rights throughout operations. Failure on this front will mean that sorely needed changes for people on the ground will not occur, and that efforts to ensure a just and inclusive transition to a green economy will be undermined. With that, we all lose"
- Climate change: the heat is on for finance directors
  "What should standards look like? Companies should disclose both their expected emissions and an assumed long-term carbon price within the scope of international averages. From that, the present cost of pollution should be calculated and stated. The European Commission is readying plans for tariffs that would eliminate the price advantage cheap imports owed to low or absent carbon taxes. This is a sign, among many others, that a global carbon price is in the offing"
- Central bank action on climate is 'imperative', says Banque de France governor
  "We cannot substitute the necessity of a carbon price, but let me stress why it is not mission creep. On the contrary, it is an imperative for us, consistent with our other mandate of financial stability and price stability. The clearest message from the NGFS [Network for Greening the Financial System] is to say that climate-related risks are part of financial risks. And so for financial institutions and supervisors as well, it's not a nice-to-have. It's not part of [corporate social responsibility]. It is a must-have and it's part of risk management"
- Central banks' action on climate change raises mission creep concerns
  "The humbling of ExxonMobil by activist investors who voted outside directors on to the board to accelerate the oil company's response to climate change raised activism to new, unexpected heights last month. Around the world institutional investors have been ramping up stewardship efforts across their portfolios, with an increasing focus on the transition to net zero greenhouse gas emissions by 2050. Yet the high tide of activism has yet to touch one group of very big public investors — namely the central banks that have accumulated large portfolios of securities since the financial crisis and topped them up in response to the coronavirus pandemic"
- Engine No 1, the giant-killing hedge fund, has big plans
  "It has been depicted as a new David-and-Goliath tale for Wall Street: a tiny hedge fund called Engine No 1 went up against the mightiest oil company in the US and won three seats on its board, with a mandate to prepare it for a future free of fossil fuel"
- Britain's steel industry faces up to the climate challenge
  "Ministers have stressed the strategic importance of the industry's role in post-Brexit Britain, but concern is growing among some executives that a comprehensive strategy to secure its future and put it on a sustainable footing is still missing"
- Europe's steel industry fears abrupt end to free carbon permits
  "Europe's steel industry has stepped up its pleas to the European Commission to ensure a level playing field for domestic producers as Brussels prepares to publish plans for a carbon border tax. In a letter sent to the commission last week, the European Steel Association (Eurofer) asked the EU not to reduce the allocation of free carbon allowances for the industry under the Emissions Trading System too quickly while the carbon border levy is being introduced"
- European airlines face big hit as cost of polluting soars
  "A sharp rise in the cost of polluting in Europe risks undermining airlines' efforts to repair their balance sheets following the damage caused by Covid-19. The cost of purchasing carbon allowances under the EU's emissions trading system, ETS, has been on a record breaking rally, with prices more than doubling to above €50 a tonne compared with pre-pandemic levels. That presents a problem for airlines in the region, which like other carbon intensive sectors must buy the tradable credits to cover the amount they pollute under parallel emissions systems in both the UK and the EU"
- Corporate-led $1bn forests scheme is 'just the beginning'
  "Amazon, Boston Consulting, McKinsey, Unilever, Salesforce, Airbnb, GSK, and Nestlé in April threw their weight behind a $1bn scheme aimed at tackling deforestation that now faces the challenge of establishing which countries will receive funds. The Lowering Emissions by Accelerating Forest Finance (Leaf) venture was launched just as new data showed greenhouse gas emissions from the loss of previously untouched tropical forests had exceeded the combined emissions from Europe's five-largest economies"

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- ESG: we're all environmentally conscious now
  "ESG funds have proved they can survive — and even thrive — in a crisis. Some $2bn a day flowed into sustainable funds in the first quarter of this year, according to Morningstar. That was half of all European fund flows into the sector. But as investors ramp up calls for sustainability at every company, and regulators set more targets for eliminating emissions, ESG has a finite future as a discrete category"

- Sustainable investing boom and net zero pledges drive ESG talent war
  "The push for businesses to be run more sustainably is driving a surge in demand for professionals with environmental, social and governance expertise, according to consultants and recruiters. More than one in five of the world's largest companies have made some form of commitment to reaching net zero emissions and investors are sharpening their focus on the social impact of companies they back, creating a boom in the market for specialists in corporate sustainability"

- US junk bond market loses steam on mounting inflation jitters
  "The US junk bond market has begun wavering on rising inflation worries, raising the risk that the powerful rally since the depths of the pandemic in the debt issued by the riskiest corporate borrowers may be coming to an end. The high-yield bond market has been a shelter for investors seeking to avoid the volatility in stocks and government bonds this year, but these riskier assets have now begun flashing signs of caution . . . In a sign of the rising angst, investors have pulled $5.6bn from mutual and exchange traded funds that buy US high-yield bonds over the past six weeks, according to data from EPFR Global, erasing inflows into the asset class from the beginning of November when successful vaccines against Covid-19 were announced, boosting markets"

- 'Game over': Investors hunt for new model after years of broad gains
  "The bond bull rally, which has pulled down yields, has meant that there are precious few sources of income left across global markets. Even European junk bond yields are now below where 10-year US government debt was a decade ago. The high prices for fixed-income assets mean bonds, typically a ballast in portfolios, are unlikely to offer much protection should stocks quake again"

- How the UK and EU are quietly diverging when it comes to financial services
  "Britain has no overarching plan for finance but rather a steady drip-drip of minor policy changes from standards agreed with the EU. The resumption of trading Swiss shares in London, tighter bank capital rules and a new prudential regime for investment firms to better reflect their risks are just the start"

- Libor's US replacements: no one rate to rule them all
  "There are many reasons why attempts to ditch dollar Libor are proving difficult. One of them is that there are multiple candidates vying to replace the doomed benchmark. The UK's Libor transition is not without its issues. But what's helped is that a consensus has formed around the Sterling Overnight Interbank Rate, or SONIA, as the agreed-upon alternative. The situation in the US is more complex, with several benchmarks all competing for the title of Libor successor. In turn, this is leading many market players to put off replacing Libor in their financial contracts as well as slowing the process to a widely approved alternative"

- Federal Reserve to unwind its emergency purchases of US corporate bonds
  "The Federal Reserve said that it would start selling the corporate bonds and fixed income funds that it bought to stabilise the financial system last year, unwinding unprecedented emergency measures that electrified markets and brought down borrowing costs for companies reeling from the pandemic"

- Global economy will return to pre-pandemic level by 2022, says OECD
  "The brightening outlook for the global economy will give governments leeway to switch from blanket emergency support to more targeted measures, with a focus on investing, the OECD has said. The Paris-based organisation said global output would rise 5.8 per cent this year, a significant upgrade from the forecast of 4.2 per cent made in December. Growth of 4.4 per cent the following year would bring most of the world back to pre-pandemic levels of activity, it added"

- Global investors pressure Asian utilities to cut emissions
  "Global investors including JPMorgan and Fidelity will demand that five of Asia's most polluting power generation companies cut their greenhouse gas emissions as part of a new climate change engagement programme. The group of investors, which has combined assets of $8.8tn, will target utilities in mainland China, Hong Kong, Japan and Malaysia that operate large coal-fired operations. Together these power companies produced roughly 285m tonnes of CO_2 in 2019, equivalent to the national emissions of Spain, according to the programme's backers. Other investors include the asset management arms of Europe's BNP Paribas and Amundi, as well as Japan's Sumitomo Mitsui"

- Chinese central bank governor backs push for climate risk disclosure
  "The Chinese central bank indicated it would throw its weight behind the development of a standardised international climate reporting framework on Friday, after starting stress testing of its financial sector in relation to the risks posed by global warming. The People's Bank of China plans to introduce mandatory disclosure of climate-related information, said governor Yi Gang, speaking at a conference hosted by the Bank for International Settlements, the so-called central bankers' bank. He did not outline a timeframe for doing so"

Regulators and Associations Monitored

1. **FCA**
2. **BoE**
3. **The Pensions Regulator**
4. **FRC**
5. **ESMA**
6. **EBA**
7. **EIOPA**
8. **ESRB**
9. **ECB**
10. **European Commission**
11. **BCBS**
12. **Autorité des Marchés Financiers (AMF) of France**
13. **CSSF**
14. **FINMA**
15. **CBI**
16. **ICMA**
17. **IOSCO**
18. **FSB**

Important Information:

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