THIS MONTH

CALL FOR EVIDENCE

While Brexit now occupies the international stage (see www.treasurers.org/node/318447), there is much activity in the EU regulation zone with a public hearing on the Call for Evidence discussed below. If you have views you'd like the ACT policy and technical team to take into account in responding to any of the subjects below, please email us at technical@treasurers.org

Steve Baseby is ACT associate policy and technical director @BasebyStephen

{ IN DEPTH }

EU public hearing on the Call for Evidence

The hearing was called to discuss the responses made to the Call for Evidence on financial services regulation. The following are observations about what was said by speakers and delegates, who included MEPs, members of the financial services Directorate of the Commission, European Securities and Markets Authority, and representatives of the financial services industry and of the real economy.

There is general agreement that the current regulatory structure needs more work, perhaps a revision of some Level 1 law, that is EU Parliamentary law, but there is a lack of quantitative data to be able to prioritise action to maximise the benefit to the real economy. What regulators ask is how customers, exports, employees and investors would benefit from further amendments to the legislation.

In the background, the EU has failed to achieve the real financial union so necessary if it wants to create a Capital Markets Union. No pan-European markets or banks have emerged to take advantage of the free movement of capital. Member states and their agencies appear reluctant to progress

and the EU appears to be in a state of stalemate, but is not considering withdrawing to a less unified system. There are neither the efficiencies of a large unified market, or the financial institutions willing to take advantage of economies of scale.

What we have is a financial system that seeks growth by pushing the economy with low rates, while not asking why there is a lack of will to invest. We have a lot of regulation that is good on paper, but untested by crises. We have a push to standardise all financial institution models, which robs the economy of diversification – a disaster if the standard proves invalid under stress.

Perhaps we have a financial system, from government to banker, which asks too much: you cannot have perfect safety and rigid rules with commercial risk taking. Someone, in regulation and banking, has to be able to make judgements. Bankers need to believe they can take commercial risk on the real economy without undue personal liability.

On liquidity

The implementation of the leverage ratio (LR) and liquidity cover ratio (LCR) are traditionally blamed for a lack of appetite by banks in cash, forex and bond trading markets, but an alternate view is emerging that historically low rates make it difficult to add lending margin. The LR and LCR lead to selective market targeting by banks as they try to achieve the high rates of return that bank shareholders continue to demand from what are now considered to be safer business models.

As a result, shadow-banking markets continue to develop to disintermediate the regulated financial institutions, and market practices continue to change. For example, export/import businesses increasingly move to open account trading as it becomes more difficult and expensive to put traditional trade finance solutions in place.

Prospectus Directive 3

The ACT has engaged with the FCA and with formal responses to consultations to ensure that the push for simpler equity and debt markets for smaller issuers and retail investors does not impact on the existing wholesale markets. The EU Parliament has understood the concerns that wholesale issuers have expressed that a simpler model, with constraints on the presentation of risk statements, could impact issuer liability. We continue to monitor developments of legislation that could come into effect by the end of 2016.

As the Deacon at Liverpool Cathedral asked at the ACT Annual Conference last month, would a modern-day institution appoint a 22-year-old to build a new cathedral? Our forebears did and the result is Liverpool's Anglican cathedral, and it is still standing and remains in use as designed. Perception of risk has altered...

Finally, we have Sven Giegold MEP to thank for noting to BNP Paribas that a bank would not lend to a real-economy business with a gearing ratio as bad as that of a bank.

View the technical updates and policy submissions at www.treasurers.org/technical and www.treasurers.org/events/webinar

Benchmarks regulation: on 28 April the EU Parliament passed legislation on benchmarks such as Euribor and Libor to make them more reliable, and to remove the conflicts of interest identified in previous means of setting interest rates. (See http://tinyurl.com/h3kj6n5)

Brexit: further resources for the 'big picture' have been added to www.treasurers.org/node/318447; and a reminder of *The Treasurer's* Brexit checklist is found at www.treasurers.org/brexit-briefing

The policy and technical team has written various blogs this month at blogs.treasurers.org

{ INTERNATIONAL }

FURTHER CHINESE MARKET REFORMS

China's efforts to increase liquidity and deter speculative trading with regulatory and market reforms have been widely reported. I have blogged on the need to retain some perspective (blogs.treasurers.org/?p=314159) with China's problems now increasingly domestic, but within a country with impressive FX reserves available to manage its economy and currency.

Measures to curb renminbi speculation may include a Tobin tax, but that there is a need identified shows the increasing liberalisation of trade in the currency.

Offshore renminbi trading

An interesting development on the international scene – as commentators try to foresee a post-Brexit world and wonder as to what would happen to euro-based business – is that London has moved into second place (from third) behind Hong Kong as the second-largest clearing centre for the Chinese currency as reported in the *Financial Times* on 28 April (see www.ft.com/cms/s/0/9fd82346-0cf2-11e6-b41f-0beb7e589515.html#axzz48Q5ICpMa) based on SWIFT data (see www.swift.com/file/25776/download?token=OoHlkSSb).

Notwithstanding the recent diplomatic flutters, the SWIFT data shows both that London has a role in the development of renminbi activity and that the currency is increasingly being used to settle trade with China.

{ WATCH THIS SPACE }

ISDA protocols and agreements

ISDA has issued further standard letters to add to its European Market Infrastructure Regulation (EMIR) Protocols. These documents are designed to ensure market participants clearly communicate their relationships under EMIR. While earlier protocols were common to all entities that are participants to derivatives (for example, the Portfolio Reconciliation, Dispute Resolution and Disclosure Protocol), some of the newer protocols are being issued at the same time as clearing rules come into force, and may not apply to all counterparties. Members are advised to refer to the ISDA site (www2.isda.org/emir) to understand which protocols and other documents they should use in the absence of bespoke amendments to ISDA bilateral agreements.

EMIR

For UK NFC+, the Financial Conduct Authority (FCA) released guidance on achieving the exemption to provide margin for intragroup transactions not otherwise cleared through a central counterparty clearing house. Members should refer to the FCA website to find out how to apply for the exemption. Also, at the hearing on 17 May, Kay Swinburne MEP acknowledged the derivative asset cross-contamination problem for NFC+, thereby opening hope for its resolution.

{ TECHNICAL ROUND-UP }

MiFID II: own account exemption reinstated for corporates

The proposed removal of the own account exemption for corporate users of trading platforms such as FXall, MyTreasury and 360T has been reinstated following representations by the ACT, the EACT and system platform providers.

IFRS: IAS 32 and notional pooling

The IASB has issued a decision on the use of offset across entities in a notional cash pool: s3.amazonaws.com/ifrswebcontent/2016/IFRIC/March/IFRIC-Update-March-2016.pdf. This will affect groups that periodically physically settle notional cash pools. The IASB's decision means that groups may not be able to account for the offset in period end accounts unless physical settlement occurs at or about the period end date. See Michelle Price's blog on the topic at blogs.treasurers.org/?p=314210

Negative rates and facility floors

Some bank facilities have zero-rate floors on the benchmark rate. Members who use interest-rate swaps to fix floating rates need to consider that the swap will not have a floor if transacted under an ISDA agreement and terms. This may create a mismatch of the floating legs if interest rates fall below zero. For those that hedge account, the impact on hedge effectiveness should also be considered.