PRIORITIES FOR THE ASSET MANAGEMENT SECTOR

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Priorities for the EU asset management policy - Roadmap for the next 5 years

The European asset management industry is evolving under the influence of technological advancements, shifting investor preferences and regulatory changes, including those relating to financial stability, competitiveness and sustainability.

The recently completed review of the AIFM and UCITS Directives aimed to enhance the efficiency of those frameworks by addressing key issues, such as to increase transparency through improved supervisory reporting, to introduce harmonised rules on loan originating funds and to improve the resilience of the sector against liquidity mismatches through harmonised rules on liquidity management tools. In a similar vein, the review of the ELTIF framework sought to boost the uptake of ELTIFs across the EU by introducing more flexible, yet robust, rules while preserving the highest level of investor protection.

These reforms constitute an important step towards boosting the resilience of the EU financial markets and contributing to the realisation of the Capital Markets Union, hence it will be essential to focus on their implementation and enforcement.

Nevertheless, as the European Commission embarks in a new mandate and sets its policy agenda for the next five years, it is the right time to reflect on the functioning of the EU legal framework and consider whether it is conducive to fostering a resilient and competitive asset management ecosystem able to support the green and digital transformation of European economies.

The European Commission will continue with its objective to reduce supervisory fragmentation and promote convergence through the development of a harmonised regulatory framework on investment funds and a continuous dialogue with national supervisors and ESMA. To that end, the recently revised frameworks and the accompanying implementing rules introduce a uniform set of rules on areas not previously harmonised at EU level (e.g. liquidity management tools, loan origination, transparency on delegation). In parallel, the Commission is contemplating to revise the UCITS eligible assets Directive. As the Directive is in force since 2007, it is deemed important to take stock of the market and regulatory developments and to consider adjustments that would minimise diverging national practices.

In line with our objective to maintain the highest standards for a robust European investment fund sector, the European Commission is assessing the merits of revising the MMF regulatory framework. Whilst the decision to review the MMF Regulation remains the in the hand of next Commission, targeted reforms such as decoupling the activation of liquidity management tools from the level of the liquidity buffers, increasing liquidity buffers or enhancing the stress tests could further strengthen the ability of EU MMFs to address systemic risks.

As highlighted by our President in her address to the European Parliament on 18 July, the European Commission is committed to promote European competitiveness, a policy objective that is particularly relevant for the asset management sector, where Europe enjoys a strong position. To that end, the Commission could reflect on further measures to facilitate the growth of the ELTIF market, including promoting the efficient and wide distribution of ELTIFs across Member States and in third countries and discussing with Member States appropriate national tax incentives. This could incentivise asset managers to channel more capital into long-term investments that support the EU real economy.

The Commission could also explore whether EU rules are sufficiently supportive of the UCITS exchange-traded funds (ETFs) to satisfy the growing investors' demand, and whether, and if so how, measures should be taken to improve the functioning and the competitiveness of the EU ETF segment.

Moreover, the Commission envisages to look at which policy measures could increase start-ups and scale-ups' access to diversified sources of private funding. As the lack of funding opportunities for late-stage scale-ups in particular seems to be a source of renewed attention, the Commission will consider whether regulatory intervention could make it easier for private investors and venture capital to finance fast-growing companies.

A framework "conducive to fostering a resilient and competitive asset management ecosystem".

Finally, subject to the steer of the next Commission, a review of the Sustainable Finance Disclosure Regulation might be warranted to simplify the framework and bring it in line with the expectations of retail investors. This could be done via the introduction of product categories which would help distinguish between products with different sustainable investment strategies. This reform would therefore contribute to deliver on the promise of simplification and competitiveness.

MARCO ZWICK
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Considerations on macroprudential policy for investment funds

The CSSF published in June a paper on macroprudential policy for investment funds. The objective is to contribute to the current discussions at international and European level on macroprudential policies and tools for investment funds, more specifically on whether to repurpose or adapt existing tools or on whether to potentially develop additional tools.

Specific and appropriate regulatory objectives apply to investment fund managers and products, in acknowledgment of justified differences existing with the regulations applying to the banking and insurance sectors: "Investment fund managers (IFMs) manage investment funds on behalf of investors who own the assets and benefit from the return of the investments on the basis of a pre-agreed investment policy and risk profile (so-called "agency model"). IFMs therefore have to comply with fiduciary obligations with the objective of acting in the best interest of their investors."

When stating that "the UCITS and AIFMD rulesets present a robust and proven framework that generally provides for the resilience of the investment fund sector", the CSSF recognises at the same time the need to address certain vulnerabilities that have been identified during recent crises.

Liquidity mismatch and leverage remain key areas of interest for investment funds. Considering the inherent characteristic of liquidity mismatch between assets and liabilities of open-ended funds, market players need to adopt a holistic liquidity risk management approach, including having access to an extensive toolbox of liquidity management tools (LMTs), as part of their usual overall risk management process, and which is available particularly for crisis management. In this context, further guidance on the selection and use of LMTs, their calibration, timing and operationalisation should be defined. It is noteworthy that the recent AIFMD/UCITS review includes amongst others the common availability of LMTs for AIFs and UCITS across the EU.

There is merit in enhancing the Money Market Funds (MMF) framework for non-government MMFs "through adapted liquidity requirements, the "releasability" of buffers in times of market tensions, the availability of anti-dilution LMTs, as well as by a decoupling of regulatory thresholds from mandatory implementation of suspensions, gates, and redemption fees, where applicable."

As part of the review of the Eligible Assets Directive, it is recommended that liquidity be systematically assessed at security level to match the fund's redemption policy, with no presumption of overall liquidity of the fund's portfolio.

The CSSF is of the opinion that IFMs should remain responsible for activating LMTs and considers that "IFMs, in charge of the day-to-day management of investment funds, are best positioned to activate LMTs, subject to guidance from competent authorities. Having authorities decide on the activation of these tools could entail significant moral hazard issues for IFMs and would in addition possibly provide the market with (unintended) signals that competent authorities see a specific market situation as being critical, and thereby possibly aggravating the situation."

As evidenced by the Liability Driven Investments episode, interconnectedness with other market participants, either via direct links or via derivatives or similar asset holdings, remains a key area to monitor for the sake of mitigating risk spreading and market tension affecting other market participants and sectors, which could ultimately result in systemic risks.

The CSSF advocates an integrated collection of supervisory data under the AIFMD/UCITS review, with an enhancement of data on leverage and a consistent definition of leverage for undertaking for collective investment in transferable securities and alternative investment funds.

To support the ultimate goal of the EU Capital Markets Union (CMU), it will hence be important to:

- avoid national/local standards which generally lead to market fragmentation;
- improve the availability and access to reliable data to increase transparency to the respective stakeholders, including investors and supervisory authorities;
- consider the international work which has recently been worked out on liquidity risk management at IOSCO, FSB and ESRB level and to which national control authorities contribute as a starting point to (i) evaluate existing tools, (ii) repurpose and adapt existing tools where necessary, and (iii) decide, after a later assessment, whether these tools are fit-for-purpose, sufficient or whether new ones should be developed.

Europe is not alone to regulate a global financial industry, such as the investment fund sector.

We must remain mindful of the fact that, in light of the upcoming CMU, Europe is not alone to regulate a global financial industry, which is in fact what the investment fund sector is. The debate needs therefore to include a thorough discussion on the competitiveness of Europe vis-à-vis other financial centres and the competitiveness of investment fund products vis-à-vis other financial products.

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CMU is an opportunity to deepen the Single Market to the benefit of everyone

The EU asset management and funds sector has developed apace since the early 2010s, with a strengthening of the frameworks including associated investor protection measures. One of the sector's key strengths is its diversity – with an assortment of products offered by a variety of providers operating across the Union. This is a model that truly represents the best of what the Single Market has to offer. It has operated well for both firms, and investors, with the potential to deliver much more for retail investors. The UCITS and AIFMD frameworks having become the references at the global level for investor protection and transparency; and recent legislative changes should improve the operating environment for firms. In this context, the EU is rightly seen as a global leader.

The AIFMD review has strengthened the funds regulatory framework and supported CMU objectives through, in particular, a harmonisation of rules concerning the availability and use of liquidity management tools, the introduction of an EU framework for loan origination and providing for enhanced data for supervisors. The availability of long-term financing is also critical to the future development of Europe's economies. The ELTIF review has the potential to significantly support this policy objective through legislative amendments that make this product more attractive from both a supply and demand side perspective.

That being said, retail investor participation in the market remains relatively low, with an estimated €33 trillion held by European consumers in deposit accounts. Some of these funds could be put to much better use, both for individual investors and society at large in terms of providing much needed capital. Accordingly, it is important that we work on measures to increase retail and professional participation, through continuing to build trust and confidence in the system.

The future of the EU asset management sector is one that is intertwined with the development of the EU capital markets. As a leading provider and regulator of financial services, Ireland strongly supports measures to build the capacity and strength of the EU financial sector. Legal frameworks need to evolve according to the policy priorities and imperatives of the day. Over the course of the last number of years there have been significant changes to the investment funds legislative framework and this is ongoing through further work on delegated acts as well as level 3 measures. While there remains a case for further reforms to the rulebook, targeted at certain fund types or activities, all in all the focus should now be on getting the level 2 rules and level 3 measures right and ensuring that the legislative changes are implemented effectively. In other words, we should not lose sight of the value of certainty and stability in the regulatory environment.

One of the sector's key strengths is its diversity.

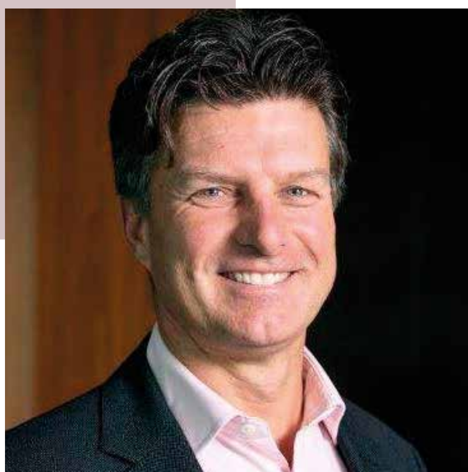
In terms of CMU, the Eurogroup roadmap from May provides a positive pathway forward with ongoing work focused at both the EU and national dimensions to ensure that an evidence-based programme can emerge.

Much has been done so far in relation to delivering this multi-year structural reform project. Over recent months, we have seen a number of important reports and high-level statements on chartering where we might go next. It is clear that CMU will be an important priority for the incoming mandate and in that context Ireland will actively work to deepen capital markets both at home and right across the EU.

There are many areas where we can expect broad support at EU level and this is where we must concentrate our efforts. Stimulating equity funding, enhancing the role of pensions, reviving securitisation markets, promoting the EU as a green finance hub and improving financial education are just some of the topics where results can be achieved.

Moreover, we should work to introduce measures which would unlock the capacity of the market to support the real economy, as well as the development of important green and digital infrastructure. In order to improve engagement with the sector, it is also important that we demystify investing for the average citizen and ensure the benefits of deeper capital markets are reaped by many. In this regard the EU asset management and funds sector should have an important role to play.

Finally, advancing the CMU project, as well as benefitting the EU internally, will allow for the improvement of European competitiveness on the global stage. The EU asset management and funds sector provides real evidence of the benefits of the Single Market for those within the EU as well as in terms of the global role that the EU plays. During the next mandate we should aim to secure our position as a global leader, remain open to capital and expertise, while ensuring financial stability and investor protection.



PATRICK THOMSON
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The partnership between policymakers and industry is the key to success

Europe's asset management industry continues to demonstrate its resilience and indeed thrive. Despite facing geopolitical unrest, uncertainty in global financial markets and the lingering effects of the pandemic, the industry has consistently delivered for investors. Recent statistics published by the European Fund and Asset Management Association show that, over 2023, all major UCITS types delivered positive – and in some cases inflation-busting – average annual performance. This resilience and success underscore the industry's ability to navigate a challenging operating environment while meeting the diverse needs of investors.

By continuously innovating, the asset manager sector ensures that end investors have the choice of and access to investment products and strategies that are best suited to their objectives. Looking ahead, we expect to see the continued rise of active exchange traded funds (ETFs), which allow investors to earn excess returns while retaining the benefits of the ETF structure. We also expect to see greater interest from retail investors in alternative and long-term assets, in light of the recently revised European Long-Term Investment Fund Regulation.

This spirit of innovation extends beyond product offerings. We are observing an evolution in the relationship between asset managers and other parts of the investment ecosystem, with the growth of bespoke partnerships that touch on everything from portfolio management to the distribution of products. One must also acknowledge the transformative impact that technology and artificial intelligence is going to have.

Nevertheless, the industry is having to contend with significant challenges on the horizon. For example, the green transition and demographic changes, which will have a profound impact on the provision of pensions. In the more immediate term, there is the need to find an engine for economic growth and the question of Europe's security. The financial services sector, and the asset management industry in particular, can play a prominent role to help identify and develop solutions to these.

As intermediaries, we support the flow of capital to the wider economy, as we identify investment opportunities on behalf of our investors. To fully harness this role, it is essential that European policymakers embrace a collaborative approach and engage closely with the industry.

As we look to the start of the next EU mandate, there is significant focus on the policy actions that will be taken by the European Commission, Council and Parliament to address some of these challenges, to further progress the Capital Markets Union and advance the EU's strategic priorities. Within this context, a key question will be on the role of legislation.

There are of course outstanding legislative proposals that will need to be completed, notably the flagship Retail Investment Strategy. As the EU institutions gear up for trilogue negotiations, we continue to encourage a shift away from equating value solely with low costs. Policymakers should instead pursue the development of an investment framework that balances investor protection with informed and responsible risk-taking. Regarding sustainable finance, particularly the Sustainable Finance Disclosure Regulation, it is clear that the status quo is inadequate, which is why we are closely following the European Commission's ongoing comprehensive assessment and their expected proposal to improve the current framework.

With regards to potential new legislative proposals, we encourage policymakers to take a thoughtful and considered approach. In short, we believe the EU would benefit from a period of regulatory stability. The flurry of legislation introduced following the 2008 Global Financial Crisis was undoubtedly necessary. Similarly, the pandemic and subsequent periods of market volatility highlighted potential gaps which reforms such as the review of the AIFM and UCITS Directives have sought to address. However, it is now crucial to allow these rules to settle and fully take effect, thereby offering stability and certainty to market participants and investors.

A stable & innovative environment will allow asset managers to continue to support the wider economy.

A stable policy and regulatory environment is also crucial when considering the current focus on improving Europe's competitiveness. As policymakers consider how this can be enhanced, it is crucial that we do not distance ourselves from the principles that have served us well to date. Europe's openness has been one of its strengths, best demonstrated by the global appeal and success of the UCITS brand. Rather than seeking to direct private capital, policymakers should instead focus on creating the optimal conditions, incentives, and product offerings to activate private domestic savings and continue to attract international capital. By fostering a stable and innovative environment, Europe's asset management industry can continue to thrive, grow, and support the broader economy.

ANDY BLOCKER
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European citizens need a more productive EU; it's time to deliver for them

Household investment rates in the Eurozone are declining.[1]

Almost 10 years on from the launch of the first Capital Markets Union Action Plan, Europeans are voting with their feet in a manner which is not, in my view, in the interest of their collective long-term financial wellbeing.

And this trend has not emerged because households do not have the money to invest. In the past two years as investment rates have declined, household saving rates have increased![2]

While the decision to hold onto cash rather than invest it could be seen as a response to the post-Covid economic uncertainty that many households in Europe (and around the world) have faced, with economic conditions normalising, inflation receding[3], and wages rising[4], there is now an opportunity – and need – to address this trend.

It is for this reason that we welcomed recent reports issued by President of the Eurogroup, Paschal Donohoe, and former Prime Minister of Italy, Enrico Letta, both of which seek to address this very issue through better integrating and improving the effectiveness of capital markets in the region and, more importantly in my opinion, making the ecosystem more productive in citizens' long-term best interests.

In this regard, it is important that Europe does not repeat past missteps in taking forward the Capital Markets Union agenda by pursuing legislative initiatives that, while well-intended, do not ultimately contribute towards a more productive capital market ecosystem.

At its core, this will require, in my view, a more pragmatic and coherent approach to the EU's often complex rulemaking process. For example, legislation should not generally have effect until the relevant underlying rules or guidance are implemented.

I also believe that the EU requires a more appropriate attitude towards investment and investment risk, and the management thereof. For example, while some policymakers have sought to provide investors with access to potentially higher-yielding assets via the ELTIF, others proposed rules which would have rendered the vehicle inoperable. It should not be the case that EU institutions operate at cross purposes in this way.[LK1] [AB2]

More broadly, developing a more attractive capital markets ecosystem will require fewer, more targeted policy initiatives, not all of which may require regulation.

First, the European Commission should maintain its efforts to coordinate Member States' implementation of financial literacy initiatives and to rollout the financial competence frameworks for citizens developed jointly with the OECD. Citizens' financial literacy should be seen as the foundation upon which the Capital Markets Union is built.

Second, policymakers should continue to support innovation and ease of access for citizens to a broad range of investment opportunities and vehicles, including private market assets, in a manner which ensures an appropriate level of protection while offering exposure to potentially more productive assets.

Third, to enhance EU citizens' long-term wellbeing at the point of retirement and beyond, where not already in place, Member States should establish autoenrollment savings plans as a supplement to, not a replacement for, state-provided or occupational pensions. Any such work on pensions should pay equal attention to both the accumulation phase and the decumulation phase, with a focus on ensuring financial security in retirement.

In support of the three policy initiatives outlined above, for those providing services to citizens in pursuit of their investment objectives and long-term financial goals, the EU needs to deliver on its ambition to maintain a more proportionate regulatory framework. The constant cycle of regulatory change must be addressed to allow firms to deliver client services more efficiently and effectively, otherwise significant resource will continue to be diverted away from the development of products and solutions which respond to clients' evolving needs.

EU investment rates are declining while savings increase; capital must be deployed more productively.

Each of these issues were referenced in the Donohoe and Letta reports and it is my sincere hope that EU policymakers can deliver on the recommendations attached to such initiatives as we move towards the articulation of the CMU 3.0 agenda.

With a new college of Commissioners and a refreshed European Parliament, it is my strong belief that policymakers must remain laser focused on addressing the trend which I highlighted at the beginning of this article and, in doing so, improving the long-term financial security and wellbeing of citizens across the region.

1. *Source: Eurostat, July 2024*
2. *Source: Eurostat, July 2024*
3. *Source: Eurostat, July 2024*
4. *Source: European Central Bank, May 2024*

SIMON JANIN
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Still a lot has to be done to reach a real Savings and Investments Union

"A concerning trend is the annual diversion of around €300 billion of European families' savings from EU markets abroad, primarily to the American economy, due to the fragmentation of our financial markets."[1] This sentence from the Letta report summarizes well the core of the challenges Europe is facing.

Indeed while savings are flying abroad, EU imports capital from the rest of the world to finance the long-term development of its businesses. This can be illustrated with the example of investments in stocks: non-euro zone equities held by residents based in the Eurozone amount to €5,724 bn. while euro zone equities held by non-residents reach €8,912 bn[2].

There are various reasons of this imbalanced situation, but two are of particular relevance for the asset management industry. The first one is the persistent lack of integration in European markets. Fragmented, EU capital markets cannot compete with their main peers. The second reason can be attributed to a bias of allocation in favor of the US market, which is notably reinforced by the evolution of market shares in the asset management sector that has evolved to the disadvantage of the EU industry. Over the past 10 years, US asset managers saw their market share in Europe rise from 27% to over 41%[3].

In view of these figures, there is urgency to help EU actors to be more competitive and unleash the significant untapped potential of investment of European savings. In 2023, these savings represented 14.02% of gross disposable income, whereas in the United States they were about 7.9%[4]. With a more appropriate framework, these huge amounts of savings could be channeled towards the financing of the European digital and green transitions.

This assessment has already led EU authorities to conduct a series of reforms as part of the EU Capital Markets Union (CMU) action plan. Notably the successful review of ELTIF Regulation should help boost long-term European investments in the real economy. Similarly, the new provisions adopted in AIFM and UCITS Directives, notably on liquidity management tools, will provide funds with even more autonomy and resilience - as long as the expected level 2 rules are properly designed.

However, a lot has yet to be done, with much stronger ambition, for Europe to become a really integrated, resilient and competitive market. In this regard, the positive momentum to relaunch the CMU project, be it renamed Savings and Investments Union, both at Members States (Eurogroup, European Council) and ESMA levels and with the conclusions of the Noyer and Letta reports should be maintained.
In particular, three key concrete actions should be taken.

The positive momentum to relaunch the CMU project should be maintained.

First, it is essential to promote more long-term investment in the EU towards retails investors. In this respect, E. Letta proposes to create an auto-enrolment EU Long-Term Savings Product. The Noyer report also puts forward this recommendation but through a European 'label' whereby each country will have the choice of creating a new product or adapting an existing one and supporting it with a tax advantage conditional to significant investments in the EU. Indeed, it is essential to make sure that products that would benefit from this label – and therefore from a tax incentive - would be predominantly invested in the EU economy.

Second, reducing fragmentation is key. This will be achieved through EU wide policies such as making sure that legal texts and their related implementation measures converge across the different Member States, without the temptation of adding burdensome local requirements ('gold-plating'). This should also be achieved through specific measures that would help pan European actors to fully benefit from more regulatory and supervisory convergence. In this respect, the recognition of the concept of group at the EU level, as notably proposed in the Noyer report, would enable European asset managers to benefit from the economies of scale generated by the single market.

Third, more attractive securitization markets could free up more capital from institutional investors. Among the proposals made by both Letta and Noyer reports, the launch of a European agency – similar to the ones existing in the US - that would provide a guarantee to securitized assets is an interesting way forward. This should be complemented by targeted reviews to the existing prudential framework. The revision of Solvency 2 in 2023 has been a promising start but this regulation, together with CRR, has to be better adapted to current market needs to enable securitization to operate at its full potential.

Although there is still a long way to go, an ambitious Savings and Investments Union could help Europe meets its challenges. Now it is time to move forward.

1. *Enrico Letta, Much more than a market, April 2024*
2. *Christian Noyer, Developing European capital markets to finance the future, Proposals for a Savings and Investments Union, April 2024*
3. *Broadridge, December 2023*
4. *Banque de France, Eurostat, July 2024*