Non-Banks: European Commission consults on macroprudential policies

22 May 2024

"NBFIs and capital markets…play a pivotal role in fostering the diversity of financial markets structure and contributing to the resilience of the financial system through private risk sharing and reduced overreliance on traditional (relationship) bank lending."

The European Commission published its planned targeted consultation this morning on **macroprudential policies for non-bank financial intermediaries** (**NBFIs**) reflecting the ever-increasing importance of the non-bank sector to the flow of capital. NBFIs comprise non-bank investment firms, asset management companies and investment funds, insurance companies, pension funds and other unregulated entities – in Q3 2023, they accounted of c41% of EU total financial assets (with banks accounting for c36%).

While the Commission is explicit that it does not want to revisit recent legislative initiatives that are close to completion (such as EMIR 3.0 and the changes to Solvency II), it notes that the scope of the consultation is wider than its mandate under Article 513 of the Capital Requirements Regulation to "*review whether the [CCR and CRD] macroprudential rules are sufficient to mitigate systemic risks*". It is also looking at whether existing tools have achieved their purpose, whether existing microprudential and reporting tools need to be repurposed or reviewed, whether new macroprudential tools (activity-based or entity-based) are needed, and improving EU-wide coordination.

Key perceived NBFI-related vulnerabilities which frame the Commission's approach to the consultation are **unmitigated liquidity mismatches** (where a liquidity mismatch is not adequately mitigated by specific tools such as liquidity management tools to withstand a plausible redemption scenario), **leverage**, and **interconnectedness** (in particular the need to understand the risks inherent in the growing interconnectedness between more traditional financial assets and digital financial assets). The importance of international coordination and looking at (through considering feedback to the Commission's targeted consultation) how to strengthen the EU regulatory framework from a financial stability perspective were highlighted by Central Bank Deputy Governor (Monetary and Financial Stability) Vasileios Madouros in his closing remarks at the Central Bank's Macroprudential Policy for Investment Funds Conference earlier this week.

The **steps taken by the Central Bank of Ireland in respect of macroprudential policies in the investment funds sector are specifically highlighted** by the Commission (such as its Discussion Paper on an approach to macroprudential policy for investment funds, the 2022 leverage limits for Irish property funds (a 60% leverage limit on the ratio of property funds' total debt to their total assets to limit liquidity mismatch), and the recent macroprudential measures for Irish-authorised GBP-denominated liability-driven investment (LDI) funds (which codified and amended the minimum yield buffer originally outlined by the Central Bank in its November 2022 Dear CEO Letter)). The consultations by IOSCO and the FSB, IOSCO's ongoing work in the area of private finance and on anti-dilution liquidity management tools, and the FSB's ongoing work in areas such as leverage, margin preparedness and vulnerabilities for open-ended funds, are also all referenced as key initiatives.

In terms of next steps, there are 68 consultation questions, and the **consultation closes on 22 November 2024**. The feedback to the consultation will inform any planning work in this area by the Commission following the June 2024 EU elections.

"*Non-bank financial intermediation plays an important role in capital markets and can support the EU's sustainability and digital agenda, where private investment will be key. A diverse financial sector is also important for maintaining financial stability, diversifying funding opportunities and reducing the over reliance on traditional bank lending*…" [EU Commissioner Mairéad McGuinness]