FSB publishes Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities

The Financial Stability Board (FSB) today published for public consultation Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities. The document sets out 14 proposed policy recommendations to address the following structural vulnerabilities from asset management activities that could potentially present financial stability risks:

i. liquidity mismatch between fund investments and redemption terms and conditions for fund units;

ii. leverage within investment funds;

iii. operational risk and challenges in transferring investment mandates in stressed conditions; and

iv. securities lending activities of asset managers and funds.

The FSB’s work to understand and address potential financial stability risks from structural vulnerabilities associated with asset management activities was launched in March 2015, in part due to recent growth in asset management activities. Asset management activities have increased significantly over the past decade, including through open-ended funds that offer daily redemptions to their investors. Such growth has been accompanied by increased investment in particular asset classes, which encompass some less actively traded markets.

Among the above four structural vulnerabilities, issues associated with (i) liquidity mismatch and (ii) leverage are considered key vulnerabilities. The recommendations for liquidity mismatch focus on open-ended funds (public and private, including exchange-traded funds but excluding money market funds). Those for leverage are meant to apply to all types of funds that may use leverage (that may arise through borrowings or through the use of derivatives). Meanwhile, recommendations for operational risk focus on asset managers that are large, complex, and/or provide critical services, and those for securities lending activities focus on asset managers’ agent lender activities (i.e. lending of securities of which an entity is not the beneficial owner), in particular their provision of indemnities to clients.

These recommendations are designed to provide authorities and asset management entities with the tools and data to effectively detect and address the identified risks. In relation to this, the International Organization of Securities Commissions (IOSCO) is also issuing today a statement on their initiative regarding the priorities for addressing data gaps related to the asset management sector. The FSB intends to finalise the policy recommendations by the end of 2016, many of which will be operationalised by IOSCO.
The FSB welcomes comments on this document. Comments should be submitted by 21 September 2016 by e-mail to fsb@fsb.org or post (Secretariat of the Financial Stability Board, c/o Bank for International Settlements, CH-4002, Basel, Switzerland). All comments will be published on the FSB website unless a commenter specifically requests confidential treatment.

Mark Carney, Chair of the FSB, stated that “The growth in market-based finance has diversified the sources of credit and investment. Given its increased importance, a resilient asset management sector is vital to finance strong, sustainable and balanced growth. These policy recommendations are designed to ensure that across the FSB membership asset managers can continue to fulfil these roles to the benefit of all”.

Daniel Tarullo, Chair of the FSB Standing Committee on Supervisory and Regulatory Cooperation, stated that “The proposed policy recommendations are designed to enhance the resilience of asset managers and funds to future stress in financial markets. They will also help authorities obtain a better understanding of the trends and risks associated with asset management activities within and across jurisdictions”.

Notes to editors

The FSB launched in March 2015 work to understand and address potential financial stability risks from structural vulnerabilities associated with asset management activities. This work has focused on: assessing recent changes in the structure of asset management activities; identifying and prioritising potential structural sources of vulnerability that could affect the global financial system; evaluating the role that existing policy measures could play in mitigating potential risks; and making policy recommendations as necessary. Separately, in July 2015, the FSB announced that it had decided to wait to finalise the assessment methodologies for non-bank non-insurer global systemically important financial institutions (NBNI G-SIFIs) until its work on structural vulnerabilities from asset management activities was completed. This will allow further analysis of potential financial stability issues associated with asset management entities and activities to inform the revised assessment methodology. The focus, in the case of asset management, will be on any residual entity-based sources of systemic risk from distress or disorderly failure that cannot be effectively addressed by market-wide activities-based policies.

The FSB has been established to coordinate at the international level the work of national financial authorities and international standard setting bodies and to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies in the interest of financial stability. It brings together national authorities responsible for financial stability in 24 countries and jurisdictions, international financial institutions, sector-specific international groupings of regulators and supervisors, and committees of central bank experts. The FSB also conducts outreach with 65 other jurisdictions through its six regional consultative groups.

The FSB is chaired by Mark Carney, Governor of the Bank of England. Its Secretariat is located in Basel, Switzerland, and hosted by the Bank for International Settlements.

For further information on the FSB, visit the FSB website, www.fsb.org.