Covid-19: Challenges for asset managers

Webinar by EFAMA and KPMG

9 April 2020
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Dealing with Business-as-unusual

Alan Picone, Partner, Advisory - Asset Management at KPMG Luxembourg
Market Pulse – in depth

- Assessment of risk tolerance & appetite in COVID19 environment
- Risk tolerance is de facto stretched
- Trade off: risk tolerance/operational continuity
- Extreme measures → NAV suspension
- Temporary measures → swing pricing
- Cannot meet two investment restrictions criteria at the same time
- Board reporting is being prepared with these in mind

- Portfolio Risk:
  - Internal risk assessment programs (supply chain, cash flows at risk, people risk)
  - Thematic funds such as market dislocation
- Valuation Risk:
  - Integration of COVID19 as a premium
  - Impairment models
  - 3rd party valuers identification

- Regulatory Continuity
- Operational Resilience
- Product Lifecycle UCITS
- Product Lifecycle AIF

- Risk Management:
  - Swing pricing
  - Liquidity analysis
  - Liquidity stress-testing
  - Ability to endure redemption shocks

- Luxembourg ecosystem relies heavily on effective delegates’ monitoring
- Managers mindful of reliance on 3rd parties
- Move from quarterly review to daily vigilance
- Review of BCPs, SLAs,
- Contractual aspects & potential litigation/disputes
Regulatory Continuity

Challenges the market players are facing

- Daily activities taking the attention from keeping up to date with new regulatory developments (e.g. AMLD VI)
- Increased regulatory obligations in terms of reporting due to communication on contingency measures due to COVID-19
- Dysfunctional patterns

How are they adapting & mitigation measures in place

- TRANSPARENCY:
  - The majority of players has shown increased attention on communications from the CSSF (e.g. FAQs issued for COVID-19 with extended deadlines)
  - They are engaging with the regulator and willing to be transparent on what they should report (e.g. investment restrictions, VaR breaches, breaches on the rules of the investment funds)
  - ManCos are finding ways to communicate properly with their boards, showing heatmaps and links of the upcoming regulation and deadlines and how these are being addressed

- DOCUMENTATION:
  - Increasingly and properly documenting the risks and mitigation measures
  - Increased disclosures to investors

- GOVERNANCE:
  - Elevated level of formalization through the recourse to internal mechanics
  - Increased frequency of decision forums → product approval, swing pricing committee, board meeting
  - Systematic Regulatory Watch

- MARKET INTELLIGENCE
  - Increased scrutiny over what is being done by peers
  - Mimicking effect and interest over who will take drastic measures
  - Increased attention over what’s being provided by consultants on market sentiment

• Not the same risks as UCITS
• Regulatory risk focused on valuation – proving that there is a proper valuation process in place
• Engage with portfolio managers to view the consequences on the portfolio companies
Operational Resilience

Challenges the market players are facing

- Business Continuity Plan covering: IT, cloud, VPN and home-office
- Data security and confidentiality
- Key people risk
- Compliance obligations
- Oversight obligations

How are they adapting & mitigation measures in place

- Majority of players have activated their BCP and are promoting home-office
- They are aware of the downsides e.g. increase in cyber criminality, risks for data confidentiality and protection
- A few players are considering relying on the cloud
- Extension of VPN capacity
- Players are reluctant to use tools that are not approved/for which there is no procedure in place
- Assessment of where resources are needed, with a view that people are not interchangeable
- Review of the Compliance Monitoring Plan that is being adapted to COVID19 actions and mitigation measures
- Improvement in the CMP for regulatory risk mitigation techniques in order to be able to demonstrate to have a proper response that is COVID19 specific
- Update risk matrix taking into account COVID 19 specific risks
- Oversight is becoming much more granular but asset managers still have a good overview on the delegated tasks
Product Lifecycle – AIFs and UCITS

Challenges the market players are facing

- Risk Management in terms of market, liquidity, counterparty risk
- Valuation risk
- Product design
- Portfolio monitoring and crisis management
- Deal sourcing and opportunities

How are they adapting & mitigation measures in place

- Majority of players have opted for a segmentation of the risk analysis, by portfolio companies – along various criteria (risk to employees, liquidity, financial, sector/geography)
- Players are taking contingency measures such as NAV suspension, measures on capital calls/drawdowns
- Increased concerns over reputation
- Valuation for UCITS concerns on the reliability of the valuation, some players are disclosing it in disclaimers informing investors of reduced accuracy in the valuation
- Valuation for PE overall reluctance to proceed with a different view on valuation
- 1-on-1 valuation reviews and most AIFMs have the intention of being more involved for the next quarter round of valuation
- Some players mention the use of Moody’s analytics credit hedge to calculate PD
- Some players are reviewing their investment range (asset class, sector, geographies) and target markets
- Majority has been actively seeking deals
- Concrete actions for crisis management:
  - Shoring up liquidity
  - Contingency planning for key people
  - Maintenance/continuation of supply chain
  - Business infrastructure and operations integrity

- Portfolio risk for AIFs:
  - internal risk assessment programs (supply chain, cash flows at risk, people risk
  - Themetic funds (market dislocation)
- Valuation risk for AIFs:
  - integration of Covid-19 as risk premium, impairment models, identifying 3rd party valuers
- Risk Management for UCITS:
  - swing pricing, liquidity analysis & stress-testing, redemption shocks
Cutting though complexity

Niamh Mulholland, Director – Regulatory at KPMG Ireland
C-19 related Regulatory Impacts

- Regulatory Extensions
- BCP/DR
- Liquidity Management
- Outsourcing
- Ensuring Business Continuity
- Regulators Communications

Regulatory Disclosures
Focus on operational efficiency and effectiveness and end-to-end continuity of customer service

Regulatory impact on existing Regulatory Requirements

- Prudential Regulation: Minimum Capital Requirements, ICAAP, ILAAP.
- Outsourcing: Ensuring effective supervision and oversight of OSPs.
- Digitalisation and IT/Cyber security infrastructure.
- Investor Protection: Minimum requirements and disclosure responsibilities under AIFMD, UCITS and MiFID II.
- Market Integrity and Individual Accountability.
- BCP/DR/Operational Resilience
Thank you!