Covid-19: Challenges for asset managers

Webinar by EFAMA and KPMG

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Dealing with Business-as-unusual

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Table of Contents

- Regulatory Continuity
- Operational Resilience
- Market Pulse
- Fund Lifecycle – AIFs and UCITS

Section 1
Section 2
Section 3
Section 4
Market Pulse - in depth

- **Regulatory Continuity**
  - 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

- **Operational Resilience**
  - 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

- **Product Lifecycle UCITS**
  - 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

- **Product Lifecycle AIF**
  - Risk Management:
    - Swing pricing
    - Liquidity analysis
    - Liquidity stress-testing
    - Ability to endure redemption shocks

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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 V)
• 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

UCITS

PE

• 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 AIFM 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
  - Thematic 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

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

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C-19 Operational Effectiveness and Resilience Considerations

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

- Technology & Innovation
- Cost & Efficiency
- Changing Threats
- Political Agenda
- Supply chain complexity
- Customer Expectations
- Incident Visibility

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
Q&A
Thank you!
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