FSB FINANCIAL STABILITY BOARD

Leverage in Non-Bank Financial Intermediation: Consultation report

Response to Consultation

Loan Market Association

Recommendation 1

1. Is the description of the financial stability risks from leverage in NBFI accurate and comprehensive? Are there additional vulnerabilities or risk dimensions related to NBFI leverage that authorities should consider for monitoring purposes?

Whilst the LMA believes that it is right for regulators to be assessing whether they have the correct information to be able to assess leverage in the NBFI universe, we would note that such universe is vast and diverse. As such, we would recommend the FSB does further diligence with the participation of different "groups" of NBFIs, with different structures, and who use leverage in a variety of ways.

For example, in the EMEA loan markets, NBFI investors use a variety of fund structures and will differ vastly in how much leverage they use as part of their investment management. However, broadly speaking, the majority of such fund structures are closed-ended and are not subject to daily investor redemption rights . As such, their ability to impact wider systemic risks is limited.

2. What are the most effective risk metrics that should be considered by authorities to identify and monitor financial stability risks arising from NBFI leverage?

Prior to proposing any new metrics on NBFIs, we would strongly urge the FSB to examine existing practices and disclosures in jurisdictions in which there is already robust data collection and risk monitoring in place. We refer to the details set out in the Consultation response to this question from the Alternative Investment Management Association ("AIMA").

3. What are the most effective metrics for the monitoring of financial stability risks resulting from:

(i) specific market activities, such as trading and investing in repos and derivatives

(ii) specific types of entities, such as hedge funds, other leveraged investment funds, insurance companies and pension funds

(iii) concentration and crowded trading strategies

Recommendation 3

4. What types of publicly disclosed information (e.g. transaction volumes, outstanding amounts, aggregated regulatory data) are useful for market participants to enhance their liquidity or counterparty credit risk management? Are there trade-offs in publicly disclosing such information and, if so, what would be the most important elements to consider? What is the appropriate publication frequency and level of aggregation of publicly disclosed information?

The LMA strongly believes that the FSB's recommendation, as it stands, would send the wrong signal to member authorities on how NBFI leverage information should be treated and distributed. The FSB has drafted its recommendation in a way that suggests disclosures "should be provided to the public" disregarding its previous risk assessment around the potential crowding around a particular entity, or activity.

Additional public disclosures, and any benefits thereof, need to be weighed against the risks of requiring disclosure of sensitive information that could adversely generate undesired market movements, potentially even adversely introducing stress in financial markets.

We recommend that the guidance of the FSB focus on limiting the sharing of entities' information privately to relevant authorities and counterparties to address the FSB's identified risks, without adversely introducing any undesired outcomes to market stability. Noting the FSB's global remit, we would also expect guidance to avoid imposing additional or different requirements in markets where there is already robust data disclosure.

In addition, while the LMA agrees with the FSB that authorities should be able to calibrate policy measures depending on the jurisdictional market structure and the relevant risks supervisors identified with respect to NBFI leverage, the LMA believes that regulatory fragmentation across jurisdictions will not achieve the FSB's objectives to ensure a more stable provision of financing to the economy and reduce the need for extraordinary central bank interventions.

Recommendation 5

5. Do Recommendations 4 and 5 sufficiently capture measures that would be used to address the scope of non-bank financial entities under consideration in this report? In what ways may the policy measures proposed in the consultation report need to be adjusted to account for different types of non-bank financial entities?

We believe it is important to distinguish between the vast array of different activities undertaken by NBFIs, as well as the diverse types and structures of NBFIs in existence. For example, a large amount of NBFI investors in the EMEA loan markets use closed-ended investment vehicles, which are not marked to market and which do not permit investors to make daily redemptions. Additionally, such vehicles are usually themselves regulated (and therefore subject to existing rules on leverage) . Furthermore, the leverage used by those entities is often bank lending (as opposed to e.g. repos or derivatives) incorporating a range of risk controls including covenants, limits and thresholds and reporting requirements.

Those structures inherently de-risk many of the systemic issues identified by the FSB in its report. Therefore, we believe it would not be proportionate to impose additional measures on such markets or their investors; a "one size fits all" approach is not appropriate for a universe as diverse as NBFIs, and the different manner in which they use leverage.

One of the LMA's key areas of focus is Fund Finance, which touches on many of these points. We would be happy to engage in further detail with the FSB on this topic, and provide more detailed insights and data.

6. **In what circumstances can activity-based measures, such as (i) minimum haircuts in securities financing transactions, including government bond repos, (ii) enhanced margin requirements between non-bank financial entities and their derivatives counterparties, or (iii) central clearing, be effective in addressing financial stability risks related to NBFI leverage in core financial markets, including government bond markets? To what extent can these three types of policy measures complement each other?**

7. **Are there benefits to dynamic approaches to minimum margin and haircut requirements, e.g. where the requirements change based on changes in concentration or system-wide leverage? If so, what types of indicators capturing concentration or system-wide leverage should the requirements be linked to?**

8. **Are there any potential unintended consequences from activity-based measures beyond those identified in the consultation report?**

9. **For non-centrally cleared securities financing transactions, including government bond repos, what are the merits of margin requirements compared to minimum haircuts?**

10. **In what circumstances can entity-based measures, such as (i) direct and (ii) indirect leverage limits be effective in addressing financial stability risks related to NBFI leverage in core financial markets?**

11. **Are there ways to design and calibrate entity-based measures to increase their risk sensitivity and/or their effectiveness in addressing financial stability risks from NBFI leverage?**

12. **Are there any potential unintended consequences from entity-based measures beyond those identified in the consultation report?**

    As mentioned above, the LMA believes there is scope for the FSB to provide more clarity on the types of entities and leverage use which should be targeted by any new measures. Again, we would note that the nature of the EMEA loan markets, and the common investment structures used therein, contain features which would prevent the emergence of scenarios such as large-scale open-ended fund redemptions and any consequential impact on broader financial market stability.

13. **To what extent can activity-based and entity-based measures complement each other? What are the main considerations around using these two types of measures in combination?**

Recommendation 6

14. **How could counterparty credit risk management requirements for leverage providers be enhanced to be more effective in addressing financial stability risks from NBFI leverage in core financial markets, such as government bond repo markets? In what circumstances can they be most effective?**

Whilst the government bond repo market (and similar markets) are fundamentally different to the loan markets in several ways, our membership includes bank entities. As such, we would note that it is important for the FSB to examine how counterparty credit risk management is already operating in certain markets (including the UK and EU). The LMA believes that existing bank regulation already imposes a sufficiently robust set of credit risk management obligations on financial institutions, and our members do not believe that any additional requirements would materially add to their existing processes and procedures.

Recommendation 7

15. **Would a minimum set of disclosures to be provided by leverage users to leverage providers be beneficial in improving counterparty credit risk management and reducing financial stability risks from NBFI leverage, including concentration risks? If so, which types of information and what level of granularity should (and should not) be included in this minimum set and why?**

16. **What are the main impediments that leverage users face in sharing additional or more granular data with their leverage providers? Is there a risk that a minimum recommended set of disclosures may lead leverage users to limit the information they share with their leverage providers to that minimum set?**

    The LMA would caution against imposing further disclosures requirements on leverage users in this context, unless leverage providers have identified material gaps in existing data. We do not believe such gaps exist, and would question the need for another set of disclosure standards imposed wholesale on financial market participants to address either non-existent or minimal data gaps.

17. **Should such a minimum set of disclosures rely on harmonised data and metrics to ensure transparency and efficiency in the use of such information for risk management purposes? Do respondents agree that such a minimum set of disclosures should be based on the list of principles outlined in the consultation report? If not, which principles should be added, deleted or amended?**

18. **Should leverage users be required or expected to provide enhanced disclosures (beyond that provided in normal market conditions) to their leverage providers during times of stress?**

    The LMA believes that enhanced disclosures in times of stress to leverage providers by NFBIs in the EMEA loan markets should only be required in limited circumstances. As noted above, loan market investment structures are often close-ended and not marked to market. As such, contagion risk across the wider financial markets is more remote.

    Our Fund Finance work can provide further insights here, regarding how bank lending to NBFI loan investment entities is structured, and how banks ensure they have appropriate controls and transparency in place.

19. **Should authorities design a minimum set of harmonised disclosures and guidelines on its application, or should they convene a cross-industry working group to do so? How do respondents believe such a standard should be incorporated into market practice? Through regulation, supervisory guidance, and/or via a Code of Conduct or similar approach?**

If the FSB ultimately concludes that such harmonised disclosures are required, we support the creation of a cross-industry working group to design such disclosures and guidelines.

Recommendation 8

20. Are there areas where the principle of "same risk, same regulatory treatment" should be more consistently applied? Are there circumstances in which the principle should not apply or should not apply comprehensively?

The LMA believes that the principle of "same risk, same regulatory treatment" be applied when requirements are tailored and not be implemented as a "one size fits all" approach. We agree with FSB that a "congruent treatment should not imply identical treatment". We also note and agree with AIMA's response to this question, which stresses the importance of assessing leverage across banks and NBFIs in a consistent manner.

LMA Loan Market Association

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Submitted via email to: fsb@fsb.org

27 February 2025

Dear Sir or Madam,

LMA response: Leverage in Non-Bank Financial Intermediation consultation (the "Consultation")

Part A: General Comments

The Loan Market Association (the "LMA")[1] is grateful for the opportunity to respond to the Consultation. As the authoritative voice of the loan markets in Europe Middle East and Africa ("EMEA"), we represent both Non-Bank Financial Intermediaries ("NBFIs") and banks which lend to those NBFIs. As such, the LMA and our members are keen to engage on this topic and ensure that any future policy measures are necessary and proportionate to any real risks present in the NBFI universe.

As an overarching comment, we note that both (i) the NBFI universe, and (ii) the different uses of leverage therein, are vast and varied. As such, we believe that prior to imposing new regulatory requirements on NBFIs and their leverage providers, the Financial Stability Board ("FSB") should delve deeper into specific sectors, markets and uses of leverage. An assessment should then be made as to whether (i) existing metrics and disclosures are sufficient to accurately assess risk in those specific sectors and markets, and (ii) whether existing measures in certain jurisdictions are adequate to address those risks.

The LMA notes that the primary use of leverage within the EMEA loan markets is bank lending to investment funds. This is different in many ways to other uses of leverage by other types of NBFIs in different markets. In particular, this use of leverage presents a substantially less material systemic risk

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[1] Since our foundation almost 30 years ago, the LMA has supported the loan markets, with a focus on enhancing liquidity, efficiency, transparency, and sustainability in the EMEA loan markets. Today, with 850+ members in 69 jurisdictions, we represent an ever-growing diversity of participants in international capital markets, including institutional investors, private and public sector issuers, banks, non-banks, technology solution platforms and market infrastructure providers, spanning the UK, the EU, the Middle East and Africa.

Through member representation on the LMA's various institutional committees and working groups, we actively engage with our members to ensure their voices are heard. Their input and guidance help shape the future of the loan markets and these groups drive the delivery of positive outcomes.

Our goal remains to ensure the loan product retains its place as a critical financing tool in the market.
For more information, please visit our website: www.lma.eu.com

to financial markets and bank entities at a more macro level. Any future guidance should take into account such differences. This has informed our responses to the specific questions below, and explains why we have not responded to certain questions.

In particular, the LMA cautions against the introduction of new activity or entity-based requirements which would not be proportional to the risks in the EMEA loan markets. Furthermore, any new disclosure requirements should be carefully calibrated, to ensure that any information being requested is of material relevance to the receivers (whether regulatory authorities or leverage providers). We do not believe it is necessary to make disclosures (whether new or existing) public; we do not believe this would contribute to any de-risking, and could potentially exacerbate adverse market movements.

Finally, we also agree with the two overarching principles set out by the US LSTA in their response to the Consultation, which apply equally to NBIF activity in the EMEA loan markets.

Part B: Specific Responses

The LMA's responses to the specific questions in the Consultation are below. We have focused on the EMEA loan markets, and it has not therefore been appropriate to respond to every question (we have retained the original numbering for ease of review).

1. Is the description of the financial stability risk from leverage in NBFI accurate and comprehensive? Are there additional vulnerabilities or risk dimensions related to NBFI leverage that authorities should consider for monitoring purposes?

Whilst the LMA believes that it is right for regulators to be assessing whether they have the correct information to be able to assess leverage in the NBFI universe, we would note that such universe is vast and diverse. Therefore, we would recommend the FSB undertakes further due diligence with the participation of different "groups" of NBFIs, with different structures, and who use leverage in a variety of ways.

For example, in the EMEA loan markets, NBFI investors use a variety of fund structures which differ vastly in how much leverage investors use as part of their investment management. However, broadly speaking, the majority of such fund structures are closed-ended and are not subject to daily investor redemption rights[2]. As such, their ability to impact wider systemic risks is limited.

2. What are the most effective risk metrics that should be considered by authorities to identify and monitor financial stability risks arising from NBFI leverage?

Prior to proposing any new metrics on NBFIs, we would strongly urge the FSB to examine existing practices and disclosures in jurisdictions in which there is already robust data collection and risk monitoring in place. We refer to the details set out in the Consultation response to this question from the Alternative Investment Management Association ("AIMA").

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[2] For example, as at December 2024, 83% of the leveraged loan markets in EMEA was comprised of CLO funds, which are closed-ended and whose investors are subject to long-dated maturities prior to the return of their investments (rather than e.g. daily, weekly or monthly redemption rights). *Source: Octus Intelligence Inc.*

4. What types of publicly disclosed information (e.g. transaction volumes, outstanding amounts, aggregated regulatory data) are useful for market participants to enhance their liquidity or counterparty credit risk management? Are there trade-offs in publicly disclosing such information and, if so, what would be the most important elements to consider? What is the appropriate publication frequency and level of aggregation of publicly disclosed information?

The LMA strongly believes that the FSB's recommendation, as it stands, would send the wrong signal to member authorities on how NBFI leverage information should be treated and distributed. The FSB has drafted its recommendation in a way that suggests disclosures "should be provided to the public" disregarding its previous risk assessment around the potential crowding around a particular entity, or activity.

Additional public disclosures, and any benefits thereof, need to be weighed against the risks of requiring disclosure of sensitive information that could adversely generate undesired market movements, potentially even adversely introducing stress in financial markets.

We recommend that the guidance of the FSB focus on limiting the sharing of entities' information privately to relevant authorities and counterparties to address the FSB's identified risks, without adversely introducing any undesired outcomes to market stability. Noting the FSB's global remit, we would also expect guidance to avoid imposing additional or different requirements in markets where there is already robust data disclosure.

In addition, while the LMA agrees with the FSB that authorities should be able to calibrate policy measures depending on the jurisdictional market structure and the relevant risks supervisors identified with respect to NBFI leverage, the LMA believes that regulatory fragmentation across jurisdictions will not achieve the FSB's objectives to ensure a more stable provision of financing to the economy and reduce the need for extraordinary central bank interventions.

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Those structures inherently de-risk many of the systemic issues identified by the FSB in its report. Therefore, we believe it would not be proportionate to impose additional measures on such markets

[3] We refer the FSB to the detailed overview of European regulation of AIFs set out on pages 4 and 5 of the Consultation response from The European Fund and Asset Management Association.

or their investors; a “one size fits all” approach is not appropriate for a universe as diverse as NBFIs, and the different manner in which they use leverage.

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Please do not hesitate to contact us should you wish to discuss this response in more detail. We would be happy to discuss any of the above responses or observations with you.

Yours faithfully,

Scott McMunn

CEO, Loan Market Association