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Spotlight on Markets – October 2023

MICA — MARKETS IN CRYPTO-ASSETS REGULATION. PREPARATIONS FOR A SMOOTH TRANSITION AND EXPECTATIONS

- Consultation on two sets of joint guidelines under MiCA
- ESG names and claims in the EU fund industry — has ESG-related language increased?
- The European sustainable debt market — do issuers benefit from an ESG pricing effect?
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ESMA in October

In this issue

Preparations for a smooth transition to MiCA — what is expected from entities providing cryptos and from national authorities

The European Securities and Markets Authority (ESMA) published a letter and a statement to encourage preparations for a smooth transition to MiCA.

In the letter addressed to the Economic and Financial Affairs Council (ECOFIN), ESMA Chair, Verena Ross, calls on Member States to designate without delay the competent authorities responsible for carrying out the functions and duties provided for under MiCA, and to consider limiting the optional grand-fathering periodto 12-months should they choose to offer it in their jurisdictions.

ESMA has also published a statement addressed to entities providing crypto-asset services and the national competent authorities that will be responsible for their supervision, which lists expectations for each from now until the end of the MiCA transitional period. The competent authorities are encouraged to dedicate resources and align their supervisory practices with those of their counterparts across the EU to begin effective supervision from day one.

Market participants are encouraged to begin planning towards a smooth transition and ensure their clients are aware of the regulatory status of their 'grand-fathered' crypto-asset offerings. The statement also reminds consumers of the risks associated with holding or investing in crypto-assets until and even after MiCA enters into application.

Background

The 'grand-fathering' period refers to the optional transitional measure under MiCA that grants Member States the ability to allow entities already providing crypto-asset services in their jurisdiction to continue providing those services from 30 December 2024 until as late as 1 July 2026 (depending on the duration chosen by Member States).

More information on the timeline for MiCA implementing measures and the transitional period can be found here.

EBA and ESMA consult on two sets of joint guidelines under MiCA

The European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA) published a Consultation Paper on two draft Joint Guidelines covering suitability assessment of members of the management body, and suitability of shareholders and members with qualifying holdings of issuers of asset referenced tokens (ARTs) and of crypto-asset service provider (CASPs). The guidance will provide clarity and harmonisation with respect to the criteria to assess the suitability of the management body, the shareholders and members with qualifying holdings, thus reducing the risk of arbitrage in the application of the rules. The consultation runs until 22 January 2024.

To foster and protect the integrity of the market in crypto assets and related services and to promote trust, it is important to ensure that the members of the management body of issuers of ARTs and CASPs as well as the persons that hold or wish to acquire qualifying holdings in them are suitable.

The draft Joint Guidelines on the suitability assessment of the members of the management body of issuers of ARTs and CASPs provide common criteria to assess the appropriate knowledge, skills and experience of members of the management body as well as their good repute, honesty and integrity and if they are able to commit sufficient time to perform their duties.

The draft Joint Guidelines on the suitability assessment of shareholders or members, whether direct or indirect, with qualifying holdings in issuers of ARTs or CASPs provide competent authorities common methodology to assess the suitability of the shareholders and members with direct or indirect qualifying holdings for purposes of granting authorisation as issuers of ARTs or as CASPs, and for carrying out the prudential assessment of proposed acquisitions.

Consultation process

Comments to this consultation can be sent to the EBA by clicking on the "send your comments" button on the consultation page.

The deadline for the submission of comments is 22 January 2024. The EBA will inform ESMA of all the comments received. All received contributions will be published at the end of the consultation, unless requested otherwise.

Background

The EBA and ESMA have received two joint mandates under MiCA to issue respectively (i) guidelines on the assessment of the suitability of the members of the management body of issuers of ARTs and of the shareholders and members, whether direct or indirect, that have qualifying holdings in issuers of ARTs in accordance with Article 21(3), and (ii) guidelines on the assessment of the suitability of the members of the management body of the CASP and of the shareholders or members, whether direct or indirect, that have qualifying holdings in the CASP in accordance with Article 63(11).

ESG names and claims in the EU fund industry — has ESG-related language increased?

The European Securities and Markets Authority (ESMA) published an article exploring the use of language related to environmental, social and governance (ESG) factors in EU investment fund names and documentation.

Tackling greenwashing is one of the key priorities in ESMA's Strategy on Sustainable Finance, and in this respect its assessment of how investment funds signal themselves (via their name or via their documents) is an important first step in the detection and monitoring of potential greenwashing.

In this study, ESMA shows that the share of EU UCITS investment funds with ESG words in their name has increased from less than 3% in 2013 to 14% in 2023. The article further highlights that fund managers tend to prefer using generic language ('ESG', 'Sustainable') rather than more specific words. This can make it more difficult for investors to verify that the fund portfolio is in line with the name.

To carry out this study ESMA has also used natural language processing techniques to examine the use of ESG-related language in more than 100,000 fund documents. As expected, funds with ESG words in their names, and as well as funds disclosing under Article 9 of the Sustainable Finance Disclosure Regulation (SFDR), tend to use relatively more ESG words in their documentation. However, the results also point to differences between the document types (regulatory document vs. marketing material), suggesting that fund managers adapt their communication based on the expected types of readers.

Background

This article contributes to ESMA's on-going monitoring efforts in the area of greenwashing risks, in particular in the investment management sector, and supports on-going regulatory efforts regarding ESG disclosure requirements for investment funds.

Webinar

ESMA organised on Wednesday, 18 October 2023 a public webinar on the article and its findings. During the webinar, authors of the article had a presentation which was followed by a Q&A session.

The webinar additionally included a presentation on the European sustainable debt market, with emphasis on the discussion if issuers benefit from an ESG pricing effect.

The European sustainable debt market — do issuers benefit from an ESG pricing effect?

The European Securities and Markets Authority (ESMA) published an article on the European sustainable debt market, analysing the existence of an ESG pricing effect ('the Greenium') across different types of sustainable-labelled debt instruments.

In the article, ESMA notes that it cannot confirm a systematic pricing benefit for any ESG-labelled debt type as of March 2023. However, issuers of ESG bonds did benefit from a statistically significant pricing in the past driven by their issuer-level ESG credentials.

The sustainable-labelled debt market

Issuance of sustainable-labelled debt has rapidly increased over the last years (+28% in one year in 1H23 and +663% since 1H18), and the variety of debt instruments with a sustainability aspect introduced to the market has increased.
Existing research suggests that sustainable-labelled debt issuers may benefit from a pricing advantage, often dubbed 'the Greenium', meaning that investors would accept lower yields in exchange for the sustainability profile of the bond or the issuer. The evidence is however not conclusive and largely focuses on green bonds only.

This article therefore analyses the existence of an ESG pricing effect for various types of ESG-debt instruments, beyond only green bonds, and further investigates if issuer-level ESG credentials can serve as an explanatory variable to explain the phenomenon. ESMA's analysis also includes an overview of the current state of play of the European sustainable debt market and provides details about how ESG characteristics have in the past and present impacted bond pricing differences. The assessment was conducted for a total dataset of 8,696 bonds from issuers domiciled in the EEA, with a combined outstanding face value of EUR 3.7tn.

As the sustainable debt market continues to evolve steadily, and considering that this analysis looks at a specific sample of outstanding bonds, these results should not be interpreted as a general rejection regarding the possibility of pricing advantages related to sustainable debt instruments. ESMA will continue to monitor these and related market developments in the future.

Background

This topic is of relevance to ESMA in terms of both its financial stability and investor protection mandate, since significant price distortions can trigger increased levels of volatility and rapid reductions in asset prices. Additionally, if issuers benefit from a pricing advantage based on a sustainability character, which proves to be inaccurate, investors may feel mislead, which can subsequently hamper investor trust.

This analysis focuses on the financial stability angle and informs ESMA's regulatory and supervisory work by assessing potential pricing distortions in the ESG debt market and thus investigating if the greenium phenomenon can trigger financial stability concerns. By doing this, ESMA aim to identify the potential for financial stability concerns at an early stage and to contribute to the ESMA strategic priority of monitoring key market developments in the area of sustainable finance.

Webinar

ESMA organised a public webinar on the article and its findings. During the webinar, authors of the article had a presentation which was followed by a Q&A session.

Decentralised Finance — market developments and the smart contracts system

The European Securities and Markets Authority (ESMA) published two articles on decentralised finance (DeFi), one on developments and risks in the EU market and another on a methodology for the categorisation of smart contracts. These articles highlight important risks to consumers, new forms of market abuse, and possible vulnerabilities to financial stability.

DeFi: developments and risks in the EU market

The article on DeFi developments and risks in the EU shows that DeFi raises serious risks to investor protection, because of the highly speculative nature of many DeFi arrangements and important operational and security vulnerabilities. Risks to financial stability are not meaningful at this point owing to DeFi's small size but require monitoring. In addition, DeFi's unique features have led to new market manipulation issues that need to be addressed.

DeFi has seen significant development over the last few years, although it remains very small in size (the Total Value Locked in DeFi protocols reached USD 45bn as of end-June 2023 representing less than 4% of the total crypto-assets market capitalisation), and has garnered attention from consumers, but also from global regulators because of the risks it raises.

DeFi: categorisation of smart contracts

The article introduces a methodology for the categorisation of smart contracts which leverages on the latter's source code and on topic modelling. It explores the rate of deployment of smart contracts belonging to the identified categories over time, contributing to an enhanced and nuanced understanding of DeFi,and also to identifying related significant risks.

ESMA defines five major smart contract categories and monitors their relative incidence over time. It notes a significant difference in terms of heterogeneity between the first and the second surge in smart contract deployment (occurring in 2017 – 2018 and in 2021 – 2023, respectively), reflecting the adoption of increasingly complex and interdependent protocols that have come to characterise DeFi.

Webinar

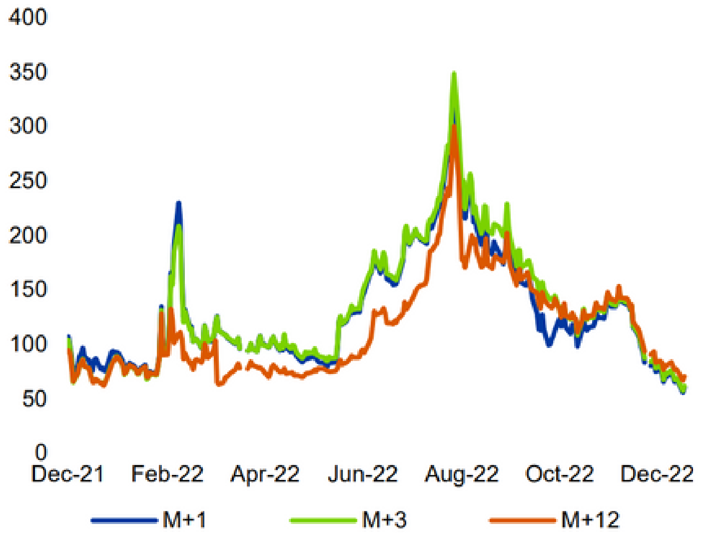
ESMA organised a public webinar on the findings of these articles. During the webinar, the authors of the articles and OECD representative delivered a presentation, followed by a Q&A session.

Natural gas futures markets in August 2022 — what happened?

The European Securities and Markets Authority (ESMA) published a study on the record surge in prices in European natural gas futures markets in August 2022. Natural gas derivative markets came into the spotlight with the Russian invasion of Ukraine, which drove uncertainty and later led to falls in Russian supplies.

Despite the record prices during August 2022, the findings presented in the study do not show correspondingly high illiquidity. CCP margins rose and fell with prices and volatility in line with expectations, with margin calls met on time. There were no signs of reductions found in derivative positions during this period. Taken together, these elements suggest that markets continued to function appropriately during the August 2022 market events.

Chart 1
European natural gas futures prices (Dutch TTF)
Surges in February and August 2022



Note: Average close price observed on ICE and EEX for selected TTF monthly contracts, in EUR.
Sources: Refinitiv EIKON, ESMA.

Strong demand was found among end-clients, with traded volumes only slightly lower than a year earlier despite the much higher prices. The focus was particularly on contracts delivering in the autumn and over the winter. Trading patterns also varied by type of market participants, such as natural gas producers, electricity utilities and banks. Findings overall are consistent with the pressing need to replenish winter reserves among European end-clients driving demand and fuelling prices, given the sharp drop in Russian pipeline supplies.

Background

ESMA analysed the record price surge by looking at market prices, volatility, CCP margins and how these related to cleared positions, available liquidity and to the trading behaviours of the larger market participants. The regulatory data were used to assess the orderly functioning of EU natural gas derivatives markets in August 2022 and complements other analyses published earlier this year (January report | March report | May article).

The study was carried out in coordination with the Agency for the Coordination of European Energy Regulators (ACER) and complements its analysis of the summer 2022 events looking at the wholesale market fundamentals and gas spot markets, as presented in ACER's annual report monitoring the internal gas market.

Analysis on the evolution of EEA share market structure since the application of MiFID II

The European Securities and Markets Authority (ESMA) published an article on the evolution of the European share market structure from 2019 to 2022, following the implementation of the markets in financial instruments directive (MiFID II). Specific focus is given to the impact of the UK's withdrawal from the EU, given its pivotal role in equity markets.

The European market structure has changed in an important manner during the observed period. The important decrease in trading volumes observed after 2021 linked to the impact of the UK withdrawal was accompanied by four main changes:

- a decrease in the number of trading infrastructures, even though their number remains elevated
- a shift in share trading distribution, both in terms of market types and countries
- a concentration of trading in a few EU countries and trading venues
- a relocation of domestic trading activities; and a rise in the specialisation of trading venues.

Background

- This topic is of relevance to ESMA in terms of both its financial stability and orderly markets mandate, since competition among trading venues can lead to more innovative services and lower fees, but a fragmented trading landscape can also impact market liquidity. In this sense, assessing the evolution of the European market structure in the recent transformative years is key to "improve the level-playing field between execution venues", which is one of the three priority areas for the Review of the Regulation governing rules about the structure of the markets in financial instruments (MiFIR Review).

European Supervisory Authorities publish joint criteria on the independence of supervisory authorities

The three European Supervisory Authorities – the European Banking Authority (EBA), European Insurance and Occupational Pensions Authority (EIOPA) and European Securities and Markets Authority (ESMA) (EBA, EIOPA and ESMA – the ESAs) – published their joint criteria on the independence of supervisory authorities.

Supervisory independence is key to ensure that fair, effective and transparent decisions are taken by appropriately resourced supervisory authorities. These authorities can in turn provide effective and adequate protection for customers and consumers of financial services ensuring confidence in the financial system. The independence criteria are organised around four key principles:

- **Operational independence:** so supervisory authorities operate without any form of undue influence from the supervised sector and the government, have adequate legal powers and operational resources.
- **Personal independence:** with transparent rules for the appointment, selection and removal of members of the supervisory authority's governing body, and high ethical standards for members of the supervisory authority's staff and governing body.
- **Financial independence:** with sufficient financial resources for supervisory authorities to fulfil their mandates.
- **Accountability and transparency:** so supervisory authorities conduct their tasks in a transparent and accountable manner.

Background

In 2020, following their review, the ESAs were tasked to foster and monitor supervisory independence.

To fulfil this task, in 2021 the ESAs published in close coordination their individual reports (Read here: EBA, EIOPA, ESMA) to take stock of the factual situation of supervisory authorities' independence. Building on these reports and based on the 2021 EIOPA's criteria and international standards, the ESAs further worked together to issue joint criteria on the independence of supervisory authorities.

Next steps

The criteria can be used by supervisory authorities as a tool to enhance their independence and, at a later stage, by the ESAs to assess supervisory independence in the EU.

ESMA expectations towards effective circuit breaker implementation

The European Securities and Markets Authority (ESMA) published a supervisory briefing on circuit breakers, which provides a comprehensive overview of supervisory expectations regarding the calibration of circuit breakers implemented by trading venues (TVs).

The supervisory briefing outlines several principles that national competent authorities (NCAs) should enforce to ensure effective circuit breaker implementation and aims to strengthen convergence among NCAs on circuit breaker calibration methodology, promoting compliance, common understanding and enforcement practices.

The guidance comes in the context of the letter ESMA sent to the European Commission about measures to be implemented in energy markets. Publishing this briefing was deemed necessary in light of recent events such as Russia's military aggression against Ukraine and the May 2022 flash crash which led to, at times, extreme volatility in commodity derivatives and equity markets.

Next steps

NCAs will inform the TVs in their jurisdiction and will follow up on the compliance of trading venues with the expectations set out in the briefing. It is expected that the calibration of circuit breakers throughout the EU will improve and therefore volatility will be better managed.

Temporary CCP collateral emergency measures extended by six months

The European Securities and Markets Authority (ESMA) extended for a limited period of six months the emergency measures which temporarily expand the pool of eligible collateral for all types of counterparties. Uncollateralised bank guarantees for non-financial counterparties (NFCs) acting as clearing members and public guarantees for all types of counterparties will continue to be temporarily eligible by central counterparties (CCPs) in order to avoid potential disruption during the upcoming cold season.

The temporary measures set out in ESMA's Final Report were adopted during the height of the energy crisis to alleviate the liquidity pressure on NFCs active on gas and electricity regulated markets that clear in EU-based CCPs.

Next steps

The Final Report has been sent to the European Commission for endorsement and will be subject to a scrutiny procedure by the European Parliament and the Council.

Publications

Click to read the news items

Date	
2 Oct	ESMA finds increase in use of ESG-related language in the EU fund industry
3 Oct	ESMA to launch Common Supervisory Action on MiFID II sustainability requirements
4 Oct	ESAs publish Joint Committee Work Programme for 2024
5 Oct	ESMA publishes second consultation on crypto market rules
5 Oct	ESMA consults on the potential impact of shortening the standard settlement cycle
6 Oct	ESMA provides analysis on issuers' potential benefits from an ESG pricing effect
11 Oct	ESMA assesses market developments in DeFi and explores the smart contracts system
12 Oct	ESMA puts forward expectations towards effective circuit breaker implementation
12 Oct	ESMA consults on possible changes to annual fees for Tier 1 Third country central counterparties
13 Oct	ESMA extends temporary CCP collateral emergency measures by six months

Date	
17 Oct	ESMA encourages preparations for a smooth transition to MiCA
19 Oct	ESMA conducts first annual assessment of Data Reporting Service Providers' relevance for EU financial markets
20 Oct	EBA and ESMA consult on two sets of joint guidelines under MiCA
24 Oct	ESMA finds natural gas futures markets functioned appropriately during the August 2022 price surge
25 Oct	ESA's Joint Board of Appeal suspends the decision by the European Securities and Markets Authority to withdraw the recognition decision of Dubai Commodities Clearing Corporation as a Tier 1 third-country central counterparty
25 Oct	European Supervisory Authorities publish joint criteria on the independence of supervisory authorities
26 Oct	ESMA signs Memorandum of Understanding with the Indonesia Financial Services Authority and recognises PT Kliring Penjaminan Efek Indonesia as Tier 1 CCP
30 Oct	ESMA publishes analysis on the evolution of EEA share market structure since the application of MiFID II
31 Oct	ESMA publishes data for quarterly bond liquidity assessment and the systematic internaliser calculations

Speaking appearances

by ESMA Staff in November

Date	
7 Nov	Sustainable finance in the EU: Regulatory Framework and Implementation - Patrik Karlsson
7 Nov	ECMI 2023 Annual Conference - Fabrizio Planta
7 Nov	ISDA Derivatives Trading Forum - Joanna Lednicka
7 Nov	Informa Meet the Expert - Isabelle Grauer-Gaynor
8 Nov	FT Live & PWM Global Wealth Management Summit 2023 - Verena Ross, ESMA Chair
8 Nov	DC Fintech Week - Verena Ross, ESMA Chair
8 Nov	ABS seminar - Thierry Sessin-Caracci
14 Nov	France Trading Conference 2023 - Carsten Ostermann
14 Nov	Sustainable Finance Summit 2023 - Alessandro d'Eri

Speaking appearances

by ESMA Staff in November

Date	
14 Nov	ELTIF 2.0 - Emmanuel Doumas
14 Nov	FT Future of Asset Management Europe - Antonio Barattelli
14 Nov	The Decade of Sustainable Finance - A half-time evaluation. - Verena Ross, ESMA Chair
14 Nov	ESBG MRC Meeting - Salvatore Gnoni
14 Nov	Meeting with the Investment Company Institute - Natasha Cazenave
14 Nov	NFSA conference/ training on Taxonomy/ report on climate matters disclosures - Eduardo Damasio & Cecile Rechatin
16 Nov	MFSA Markets in Crypto-Assets Regulation - Verena Ross, ESMA Chair
16 Nov	Roundtable - Natasha Cazenave
20 Nov	Meeting with the Financial Services Committee of the American Chamber of Commerce to the European Union (AmCham EU) - Roxana de Carvalho

Speaking appearances

by ESMA Staff in November

Date	
21 Nov	XIV Corporate Governance Conference - SAE - Valerio Novembre
21 Nov	RegTech Convention 2023 - Joanna Lednicka
21 Nov	Financial Regulatory Authority Public Conference: Fintech and Sustainability: Threats or opportunities - Klaus Löber
22 Nov	International Financial Standards Conference 2023 - Fabrizio Planta
23 Nov	AMF - 20th Anniversary conference - Verena Ross, ESMA Chair
23 Nov	BEUC Conference "Back to the Future: the promises and perils of digital finance" - Natasha Cazenave
24 Nov	29th Annual Conference - Verena Ross, ESMA Chair
27 Nov	Workshop on DORA - Barbara Daskala
28 Nov	18th European SSM Round Table - Steffen Kern

Speaking appearances

by ESMA Staff in November

Date	
28 Nov	Marché boursier 2023 – 2024 : que retenir ? Qu'attendre ? - Natasha Cazenave
28 Nov	FIA Asia conference - Klaus Löber
29 Nov	Annual Nordic Financial Ecosystem Forum conference - Jakub Michalik
29 Nov	20th Annual FIMA Flagship Conference - Fabrizio Planta
30 Nov	Irish Funds UK Symposium - Antonio Barattelli
30 Nov	ESBG Retail Banking Conference 2023 - Evert van Walsum

Consultations

Click on the consultation

Closing date

10 Nov Consultation on the review of Tier 1 CCP fees

Hearings and Webinars

Did you miss our latest hearings and webinars?

25 Oct Webinar on the findings of the articles on decentralised finance

presentation

18 Oct Webinar on ESG names and claims in the EU fund industry, and ESG pricing effect

presentation

7 Sept Webinar on ESMA's report on trends, risks and vulnerabilities no. 2, 2023

presentation

Open vacancies

All open vacancies can be found on ESMA's recruitment portal

Deadline

22 Nov	Senior Policy Officer (digital finance and innovation profile)
22 Nov	Senior HR Officer
24 Nov	Legal Officer (enforcement profile)
31 Dec	Seconded National Experts (multiple profiles)
31 Dec	Traineeship Notice - Support functions profile
31 Dec	Traineeship Notice - Economics, Data and IT profile
31 Dec	Traineeship Notice - Regulation, Supervision and Policy profile

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