Deloitte.

Recover, renew, rebuild

Financial Markets
Regulatory Outlook 2021

CENTRE *for*
REGULATORY
STRATEGY
EMEA

‘...we have a once-in-a-century opportunity to build forward better. Simply returning to the low-growth and high-inequality economy of the past is no longer an option.’

Antoinette M. Sayeh, IMF Deputy Managing Director, 15 December 2020[1]

‘The challenges of the pandemic are daunting, but this crisis presents us with opportunities too. Opportunities to reshape our financial system to make it fit for the recovery and provide more sustainable investment and credit in the years beyond.’

Charles Randell, Chair of the FCA and PSR, 16 June 2020[2]

Global foreword

The world continues to face a formidable shared challenge in COVID-19. Yet the economic implications of the pandemic – along with government and regulatory responses – are increasingly variable between regions. Regulators and financial services (FS) firms have naturally prioritised financial and operational resilience, and navigating these critical challenges is no mean feat, particularly amid a continuing degree of regulatory divergence between jurisdictions.

Thus far, regulators have worked closely with FS firms to ensure they are a key part of the solution in pandemic responses [Figure 1]. Firms will understandably want to preserve this role. First and foremost, this means fulfilling the industry's primary function: channel credit and investment to where they are most needed. But FS firms will also need to deliver in three important areas: the increasingly urgent need to progress against sustainability objectives, fostering cultures that deliver good outcomes for customers and society, and making meaningful progress on the imperatives of diversity and inclusion.

These issues form the context of our *Regulatory Outlook 2021*, which we expand on in this global foreword, before turning to our respective regional concerns (United States, Asia Pacific, and Europe, Middle-East, Africa).

Financial resilience amid a bleak economic outlook

The market turmoil in early 2020 left central banks with little choice but to respond decisively to restore stability and order to financial markets. Thereafter the defining feature of central bank responses to the pandemic has been the increase in credit provided to the non-financial private sector, and the levels of public sector assets held [Figure 2].

Following sharp drops in GDP, 2021 will likely see a return to growth worldwide, albeit at variable rates. GDP in the Asia Pacific region is forecast to grow by as much as 6.9% this year,[3] though the US and parts of Europe will continue to grow more slowly, particularly as at the time of writing parts of Europe are re-entering or extending stricter national lockdowns. Even with this growth, world GDP will nevertheless remain below pre-pandemic forecasts [Figure 3], and the road to recovery remains extremely fragile.

Though Jay Powell, Chair of the US Federal Reserve Board (FRB), characterised progress on vaccines as 'good and welcome news', he noted that it remains too soon to assess the implications for economic recovery.[4] The challenge facing policymakers is bridging the gap until the roll-out of vaccines is further advanced and the recovery can build its own momentum.[5] In many countries, interest rates look set to remain low - or even go to negative - for an indeterminate period [Figure 4], compounding existing profitability challenges for FS firms.

Central bank actions coupled with widespread government fiscal support measures have helped cushion the blow to the real economy and financial markets, albeit raising concerns about elevated (and in some cases unprecedented in peacetime) sovereign debt levels [Figure 5].

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Global foreword

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Many challenges lie ahead for the banking sector, with significant credit losses appearing inevitable in 2021 as some governments unwind their support measures.

We expect bank supervisors to take heed of lessons learned the hard way in Europe during the last decade and encourage timely recognition of impairments. We also expect a continued emphasis on the ability and willingness of the insurance industry to contribute to economic recovery by paying out pandemic-related claims where there are reasonable grounds to do so, with policymakers in jurisdictions including the UK and the US pushing for insurers to pay out COVID-19 related business interruption claims.

The prudential regulatory reforms that followed the Great Financial Crisis (GFC) have undoubtedly helped firms weather the initial storm, and have so far passed their first real test. Stress tests around the world[6, 7, 8, 9] suggest that the financial sector as a whole should be able to withstand very significant pandemic-induced losses. Nevertheless, the level of uncertainty remains high, and it is likely that some firms may fail, particularly at the smaller end of the spectrum.[10] In some more severe scenarios credit and valuation losses - combined with continued unprecedentedly low interest rates - could put some firms' capital positions under substantial pressure.

When it comes to appraising the effectiveness of the regulatory framework through the pandemic, attention will focus once again on systemic scope and resilience, the perimeter, and any threats posed by the non-bank financial sector to financial or market stability. To this end, as legislators, central bankers and regulators reflect on the resilience of markets to disruption and the effectiveness of their toolkits, more stringent regulation of certain types of investment funds and other non-bank financial institutions is in prospect.[11]

Operational resilience in a post-pandemic digital world

The global financial system may have coped well with the operational disruption caused by the pandemic. Still, supervisors will not allow firms to rest on their laurels, reiterating the message that the pandemic does not represent the most severe form of operational stress for which firms should prepare.[12] Anticipated acceleration of firms' digitisation and automation activities due to cost pressures and changing customer demands also put operational resilience front and centre. Cloud migration remains a key enabler for digitisation. As more firms move to the cloud, long-standing regulatory concerns around the systemic importance of Cloud services providers will become more pertinent than ever. In the US, one recommendation to the incoming administration is for the Financial Stability Oversight Council to consider designating cloud computing companies as Systemically Important Financial Markets Utilities.[13]

We expect regulatory initiatives on operational resilience to accelerate worldwide at the international and national level in 2021. Cross-border groups which implement a global approach to operational resilience will need to accommodate differences in emphasis - and in some cases substance - between national regimes, adding cost and complexity to the process. In the US, recent guidance from the

Global foreword

FRB calls for federal banking examiners to review the use of remote work technologies and teleconferencing systems for work-at-home arrangements, along with the elimination of physical controls present in many office environments.[14]

Dealing with divergence

Indeed, despite the common strategic and regulatory challenges facing the FS sector worldwide, divergence in the regulatory detail is increasingly the norm. Ninety-one percent of respondents to a recent Deloitte survey have observed at least some regulatory divergence across global jurisdictions that has affected day-to-day operations.[15] For many firms operating in Asia-Pacific coping with divergence is part of business-as-usual, but elsewhere there are new divisions for firms to deal with (most notably EU/UK divergence through Brexit).

The pandemic has effectively provided an ongoing stress-test of the regulatory framework developed since the GFC. Legislators and regulators will likely consider the effectiveness of those reforms, alongside their temporary pandemic response measures. There is an opportunity to avoid divergence through global coordination, but the prospect of this may be slim, particularly given that the rollback of temporary measures will depend on local economic conditions, which will vary regionally.

Looking forward

Looking ahead, FS firms will continue to have to make difficult decisions due to the highly uncertain economic outlook. Yet they will also seek to play their role in the economic recovery. Insurers and investment management firms in particular should consider contributing long-term capital towards supporting small and medium enterprises and infrastructure projects, providing funding to certain illiquid assets that create real long-term value. Banks will also be looking to maintain the flow of credit to the real economy.

In fulfilling these roles, however, we see three crucial areas in which we expect regulators as well as society to scrutinise the performance of FS firms. For FS leaders to continue to be regarded as part of the crisis solution, they will need to demonstrate progress in addressing these challenges.

Supporting sustainability objectives: FS firms have an opportunity to help society tackle climate-related risks in their role as investors, advisers, lenders to the real economy and insurers of catastrophic risks. Authorities will want to enable green finance to help 'build back better' and accelerate the transition to a net-zero economy. The taxonomies being established in jurisdictions such as Canada, the EU and China will provide a useful starting point to support FS firms investing sustainably. Meanwhile, regulators worldwide are developing climate stress tests, while also pushing firms to develop their own capabilities to assess their financial resilience against climate risk. In the US, the sustainability agenda is expected to accelerate with the incoming administration. Environmental, social and corporate governance disclosure requirements are also becoming more prominent, and increasingly mandatory globally, though any convergence towards a coherent set of global standards will likely be slow.

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Global foreword

Creating cultures that deliver good customer outcomes and embrace social purpose: regulators will pay increasing attention to firms' treatment of customers experiencing financial distress as the effects of the pandemic linger, particularly as support measures are withdrawn. To continue to be regarded as part of the solution, firms will need to be flexible in dealing with their customers, considering the appropriateness of further forbearance and engaging with customers proactively before payment breaks end. The extent to which FS cultures deliver good customer outcomes through the next phase of the pandemic will bear heavily on judgements about how FS firms have performed and any associated reputational risks.

Diversity and inclusion: diversity and inclusion rose rapidly up the agenda around the world in 2020, through social movements. In the US, the FRB has devoted considerable attention to addressing social injustice issues and reducing racial inequalities. In Europe, regulators are reinforcing commitments to diversity and inclusion as a means of improving governance, culture and practical decision-making in FS. Firms will need to demonstrate to regulators, including through data and management Information, their progress towards achieving more diverse and inclusive boards and workplaces.

Conclusion

This, then, is our view of the backdrop for 2021. Economic prospects remain highly uncertain and variable between regions, while significant downside risks remain. For regulators, ensuring the ongoing financial and operational resilience of FS firms, so that they continue to meet the needs of their customers and the economy overall, will remain paramount. But the industry will also need to prioritise progress on sustainability, culture, diversity and inclusion if it is to play its full role in helping customers and society responsibly navigate this unprecedented environment. We cannot understate the magnitude of the risks facing firms in 2021, but therein lies an opportunity for firms to lay the foundations of their future success.

Tony Wood
Centre for Regulatory Strategy
APAC

Irena Gecas-McCarthy
Centre for Regulatory Strategy
Americas

David Strachan
Centre for Regulatory Strategy
EMEA

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Global foreword - Figures

Figure 1: Bank lending to the non-financial sector[16, 17]

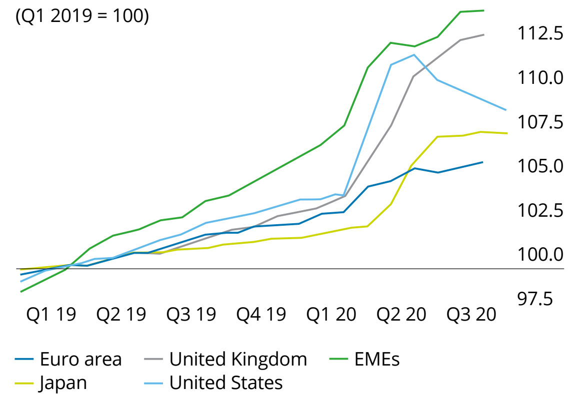


Figure 2: central bank responses to the GFC vs. COVID-19 crisis (% of pre-crisis GDP)[18, 19]

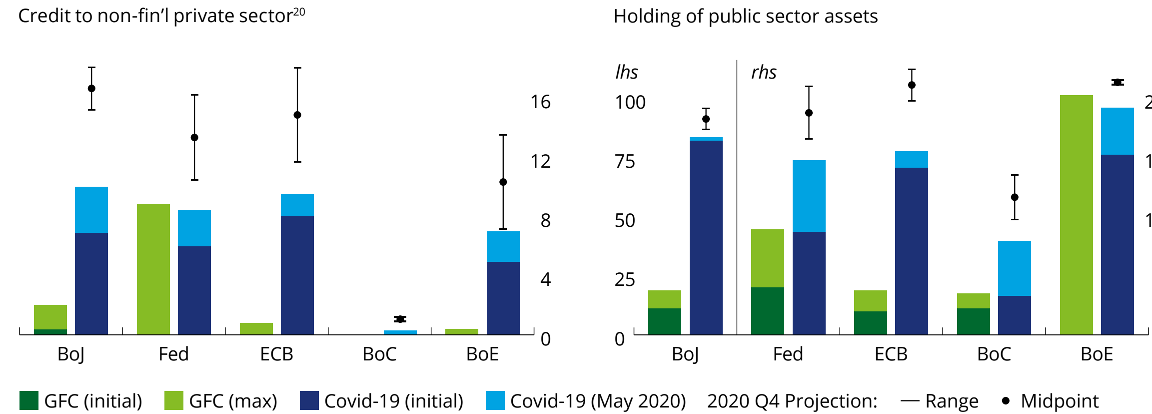


Figure 3: GDP in 2021Q4 relative to November 2019 projection % difference[21]

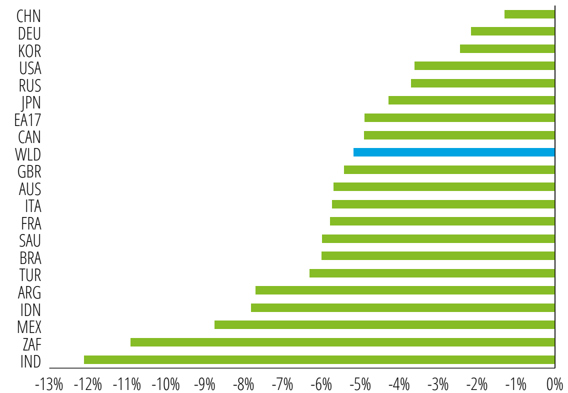


Figure 4: Global central bank policy rates[22]

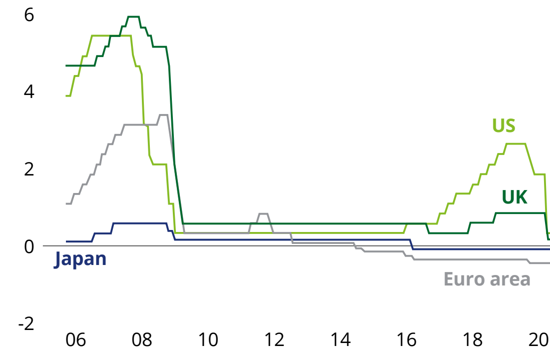
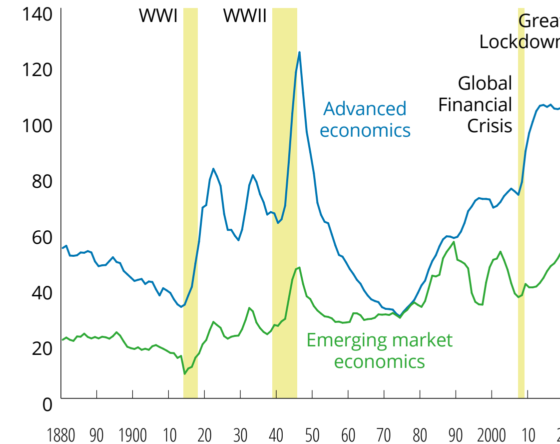


Figure 5: Historical patterns of general global debt percent of GDP[23]



Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Introduction

Our *Regulatory Outlook 2021* from the EMEA Centre for Regulatory Strategy sets out our view of the trends, specific regulatory themes and the impact of COVID-19 that will shape FS in 2021. The document is structured around nine themes that emerged from our analysis, briefly summarised below, and explored in more depth in our report.

Theme	Summary
Credit risk, financial resilience and business model viability	Concerns around credit quality following COVID-19 have raised questions about the near-term financial resilience of the FS industry and the long-term viability of some business models. 2021 will see firms trying to manage credit impairments, implement recovery measures, work to maintain financial resilience, and pivot their business models to respond to the 'new normal'.
Final call for IBOR	The transition away from IBOR has entered what should be, for the most part, its final year. There remains a risk of disorderly transition, in spite of the tools available to the authorities to manage the process. We are likely to see a range of different rates in the market in January 2022, with full international alignment within industry or between regulators unlikely.
Brexit – beyond the transition period	With the Brexit transition period having ended, FS firms have no choice but to continue building out new EU presences. We do not expect significant slow-down in activity as supervisors press banks to deliver on the substance agreed in their authorisation plans. We also anticipate increased EU supervisory pressure for certain clearing activity to migrate to the EU bloc.
Sustainability	Regulatory work on sustainability has continued throughout the pandemic. Regulators continue to progress various climate-related stress test initiatives, while at the same time pressing firms to integrate ESG considerations fully into their risk management frameworks and business strategies.
Conduct, culture and governance	We expect increasing supervisory focus on firms' cultures and quality of governance in the light of the pandemic. Supervisors expect firms to promote cultures that seek to achieve good customer outcomes and recognise wider social expectations. At the same time, firms face rising balance sheet risks and continued pressure to manage their finances responsibly, resulting in a potential tension between conduct and prudential regulatory objectives.
Deploying digitisation and innovation	Digitisation and technological innovation will be a key driver of economic recovery and growth, with digital consumer habits formed throughout the pandemic here to stay. Industry must be sensitive to the supervisory concerns raised by the speed and urgency of digitisation, including issues such as operational resilience, conduct and prudential risks in payments, and the use of AI and big data analytics.
Financial crime in the new normal	Regulators are now concerned that the mass shift to remote working following the pandemic has materially altered - or facilitated - patterns of financial crime. The near-term supervisory priority will be to ensure firms maintain robust risk and control frameworks in this 'new normal'. We expect regulators to use existing accountability regimes robustly to help deliver this.
EU/UK regulatory divergence	Across all sectors, there are a number of big ticket items where we know that the UK's regulatory approach will diverge from the EU's in the year ahead. For the banking sector, this will be particularly pertinent in the case of Basel 3.1 and CRD5 implementation. Meanwhile for insurers, material divergence from the more contentious areas of Solvency II implementation is likely, particularly the risk margin, MA eligibility and model approval approaches.
Operational resilience	Supervisory attention will focus on ensuring that firms have taken stock of lessons learnt in the first wave of the pandemic, and are prepared for future waves and associated disruption. The fact that firms generally remained operationally resilient throughout the pandemic will not in itself satisfy regulators, who will ultimately require firms to consider still more challenging operational disruption scenarios.

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Cross-sector themes

Credit risk, financial resilience and business model viability

Final call for IBOR

Brexit – beyond the transition period

Sustainability

Conduct, culture and governance

Deploying digitisation and innovation

Financial crime in the new normal

EU/UK regulatory divergence

Operational resilience

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Credit risk, financial resilience and business model viability

Overview

The unprecedented economic downturn has raised concerns about credit quality, creating challenges for financial resilience and business model viability. A true picture of losses will not be clarified in 2021 – this process will play out over a longer period – but these, together with interest rates at new lows and negative rates in prospect or already in place, are exacerbating existing profitability challenges. The pandemic has accelerated the need to reshape business models, including through digital transformation. 2021 will see firms trying to manage credit impairments, implement recovery measures, work to maintain financial resilience, and pivot their business models to respond to the 'new normal'.

In focus

- NPLs and expected credit losses will rise in 2021, but will not yet carry through fully to bank capital ratios, as a result of the extended IFRS 9 transition and the length of default and recovery processes.
- Supervisors will push for more proactive NPL resolution strategies, but efforts to introduce an EU-wide network of AMCs to take NPLs off bank balance sheets will not bear fruit in 2021.
- Despite ongoing work by the ECB and EBA, widespread cross-border bank M&A remains a distant prospect, but domestic mergers will continue.
- EIOPA is unlikely to declare a sector-wide 'exceptional adverse situation' unless further economic deterioration causes widespread, substantial drops in insurers' solvency positions.
- Reforms to the insurance risk margin will progress in the EU and UK, mitigating pressures on the cost of capital.
- Investment fund liquidity issues will be high on the regulatory priority list, with changes to redemption windows or the introduction of 'swing pricing' expected in the UK.

Credit risk and financial resilience

Sizeable credit losses appear inevitable, affecting banks' loan books, and insurers' and investment managers' bond and property portfolios. Nevertheless, the range of potential outcomes remains disconcertingly wide, with material uncertainty about the trajectory for unemployment and economic growth, and the medium-term viability of sectors such as travel, hospitality and commercial property.

The banking sector is well placed from a capital and liquidity perspective [Figure 6], even in the face of sizeable losses [Figure 7], but navigating current volatility remains challenging. Judging fundamental asset quality and the impact on capital is difficult with the true picture partially obscured by governments' economic support schemes, and the lack of historical precedents.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Credit risk, financial resilience and business model viability

Figure 6 – European banks remain well-placed from a capital perspective[24]

EU & UK banks' CET1 ratios (Q1-Q3 2020)

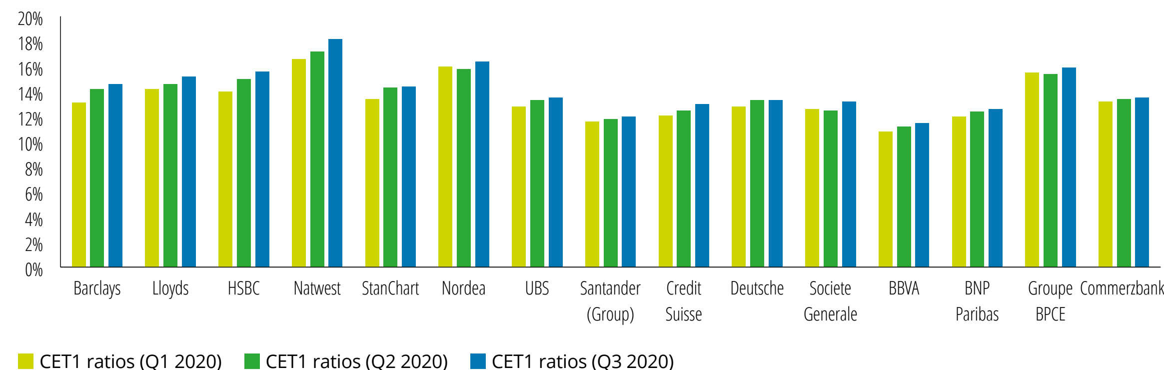


Figure 7 – expected credit losses for banks

The true picture of losses will remain elusive in 2021; IFRS 9 requires recognition of expected credit losses as conditions worsen, but the default and recovery processes determining actual losses will extend beyond 2021. Furthermore, provisions for expected losses can continue to be fully added back to capital under IFRS 9 during 2021, implying that capital ratios may not fall significantly this year.

The decline in credit quality nevertheless entails a build-up of NPLs, with more customers entering into forbearance, default or recovery processes. Regulators are instigating a more proactive NPL resolution strategy than in the previous decade, pressing banks to recognise impairments early. Banks must tread a fine line through these credit decisions, particularly in light of conduct expectations that they should allow time for customers to make payments. We do not expect proposals for an EU-level network of AMCs ('bad banks') to remove NPLs from balance sheets to gain near-term momentum, although national AMCs will be used where they exist, or may be newly established. And while the EU's accelerated Capital Markets Recovery Package has the potential to make NPL securitisations more attractive, neither securitisation nor AMCs are a panacea. Banks will need to invest in their operational capacity to deal with elevated volumes of NPLs, including digital capabilities for collections; those that can process more and better quality data will be better able to rebalance portfolios.

To prevent a contraction in credit availability, regulators have emphasised that capital buffers can be used to support new lending,

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

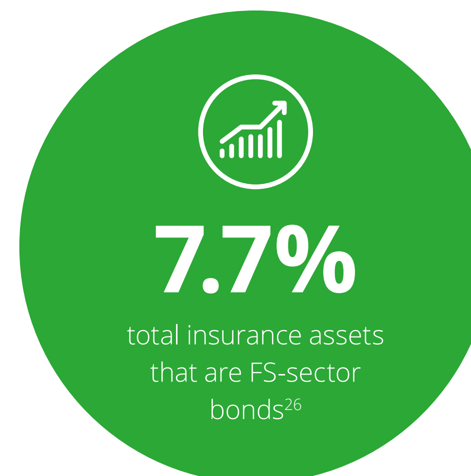
Credit risk, financial resilience and business model viability

but banks will be reluctant to dip into their combined buffer requirements. For the time being, this question remains moot as bank capital ratios generally increased during 2020, partly as a result of regulatory restrictions on distributions. The PRA and ECB have indicated that banks can resume distributions, but only within certain parameters that will mean the value of distributions during 2021 will remain low. Indeed, the PRA was explicit in noting that distributions (even within the parameters set) should not impede banks' ability or willingness to lend, while the ECB requested that banks consider not making any distributions until the end of September 2021.

The deteriorating credit environment will affect insurers and investment managers through ratings downgrades or defaults on corporate bonds and securitised loans [Figure 8]. There remains a risk of a spiralling cycle of downgrades leading to sector-wide portfolio rebalancing and price drops, further weakening asset valuations. However, although insurers' strong solvency position has weakened to some degree following COVID-19, major portfolio rebalancing is not yet in evidence. EIOPA stands ready to declare a sector-wide 'exceptional adverse situation' if needed, which would give more time to insurers to recover their solvency levels. However, we do not anticipate such a declaration unless a significant number of firms appear likely to breach SCR, which would only follow a substantial further economic deterioration. In the meantime, insurers will be expected to update metrics to manage potential credit risk exposures through corporate bonds, and identify clear management actions in case of breaches. Insurers with exposures to long-term, illiquid investments affected by the downturn, such as property exposed to travel and retail, will need to invest in workout and recovery teams to manage impairments.

The downturn will add weight to EIOPA's longstanding recommendations to introduce new rules on recovery and resolution for insurers, and for EU harmonisation of insurance guarantee schemes. In this regard, we expect movement from the Commission on guarantee schemes, with material steps towards EU-wide harmonisation likely, but only minor adjustments within the Solvency II framework rather than a recovery and resolution framework mirroring that on the banking side.

Figure 8 – insurance corporate bond exposures remain elevated



Investment managers will be focussed on the channels through which market-wide distress could make them vulnerable, particularly liquidity issues that could result in funds being 'gated', closed or liquidated.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Credit risk, financial resilience and business model viability

In anticipation of this, regulators will expect investment managers to formulate liquidity plans and review potential trigger points to shutter individual funds. Overall, the sector, in particular its potential systemic impact, is under increased regulatory scrutiny as a consequence of the market turmoil of March 2020. More stringent regulation of certain types of investment funds and other non-bank financial institutions is in prospect, as evidenced by the FSB's recent review of the market turmoil of 2020, and forthcoming changes in the UK to address liquidity issues.

Business model viability and recovery

Many FS firms faced structural profitability challenges prior to COVID-19, and the pandemic has compounded weaknesses, necessitating restructuring and business model transformation, such as the need for digitisation.

For banks, credit impairments will eventually hit capital, while low, zero, and in some countries negative interest rates continue to compress margins and depress returns on sizeable liquidity portfolios. Organic capital generation will be extremely difficult, and major cost reduction exercises will continue. The EBA and ECB advocate consolidation to reduce excess banking capacity and cut costs, and while they are working to address regulatory barriers, these nevertheless remain. Coupled with the poor macroeconomic environment, major cross-border deals remain a distant prospect, although in-country bank mergers will continue.

> 'Many FS firms faced structural profitability challenges prior to COVID-19.'

Negative rates are biting across Europe, and their deployment in the UK is a real prospect. We observe a growing willingness in principle to pass negative rates to broader ranges of customers, with size thresholds on deposits being charged negative interest coming down. If the UK opts for negative rates in 2021, banks will look to offset squeezed margins through new or increased fees, including for some currently 'free-if-in-credit' accounts. Negative rates also pose challenges for IT systems and other operational issues, such as the need for widespread customer engagement, requiring both time and investment.

The path to recovery will be uneven, and some weaker banks will become targets for acquisition or exit the market. Smaller or less diversified banks – including some digital players – will struggle more than large incumbents. Indeed, the uptick in volatility has particularly benefited some groups with investment banking arms, and while volatility may not be as elevated in 2021 as in 2020, diversified business models will remain beneficial. The pandemic has accelerated digitisation, but the smaller scale and less mature business models of digital challengers leave them with fewer options to navigate the current environment. Digital players will need to adjust their business models, for instance through more fee-based products, and demonstrate to supervisors that they have a plausible one-to-three-year path to profitability.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Credit risk, financial resilience and business model viability

For general insurers, pandemic-related claims losses will draw on capital, but will also drive price increases. These, coupled with the relatively attractive yields, will attract investors' capital into the sector. Technical pricing will need to capture pandemic-related loss experiences from 2020. Supervisors will scrutinise pricing and reserving adequacy, as well as the clarity of policy wording around these risks. Low and negative interest rates will continue to put pressure on solvency and eat into insurers' investment income, particularly for life insurers offering annuities and long-term guarantees. But, 2021 may provide some respite, with reforms to the risk margin likely to progress in both the EU and UK. Insurers will consequently need to re-evaluate strategies for managing the risk margin and low interest rate environment; this will be complex, particularly with concurrent reforms underway on long-term discounting.

We expect to see the first 'superfund' transaction in the UK pensions sector in 2021, reflecting an investor view that from a cost synergy perspective 'bigger is better'. This will enforce the need to establish clear interactions and cooperation mechanisms between the PRA's and TPR's regulatory frameworks, and raises the potential for commercial pressures to develop in the BPA and insurance buy-in market over time. We expect lobbying to try to put capital standards between insurers and superfunds on a more equal footing, even though reform of the risk margin would effectively materially reduce capital requirements for annuity writers. There is likely to be a longer-term debate on aligning the capital regimes in one direction or another, though this will not conclude in 2021.

For investment managers, generally lower market valuations – although US indices have reached record highs – will compress fee income and create further pressure towards consolidation. Specialist investment managers with significant exposures to leveraged companies and distressed or sub-investment grade quality debt will struggle if there is a sharp rise in defaults, as will funds with exposure to industries hardest hit by the pandemic. The sharp impact on corporate profitability and dividends is likely to lead investment managers to increase their offerings of alternative assets to meet investor expectations, leading supervisors to scrutinise their inherent value for money and whether the increased volatility and liquidity risks are being adequately communicated.

'Low and negative interest rates will continue to put pressure on solvency and eat into insurers' investment income.'

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Final call for IBOR

Overview

The transition from IBOR has entered what should be, for the most part, its final year. Firms – and particularly banks – can expect sustained supervisory pressure, particularly to cease issuance of GBP LIBOR-linked products with post-2021 maturities by the end of Q1, and to convert the greatest possible volume of GBP LIBOR-linked products through Q2 and Q3, while providing continuous data to supervisors to evidence their management of conduct risks. There will inevitably be a tough legacy residual, most likely in our view to be complex derivatives, syndicated debt, certain floating rate notes, and preferred stock issuances. Client engagement is crucial, with banks needing to secure buy-in to ISDA's fallbacks protocol, and insurers and investment managers needing to increase their engagement with the process, understand their exposures and work through the risks with their stakeholders. There remains a risk of a disorderly transition, in spite of the tools available to the authorities to manage the process. Either way, there is likely to be a range of different rates (new RFRs and existing or modified IBORs) in the market in January 2022, potentially creating confusion, increasing basis risk and fragmenting liquidity.

In focus

- EUR and CHF LIBOR look set to cease at the end of 2021. Some tenors of GBP and JPY look set to remain, although possibly with revised methodologies. One week and two month USD LIBOR will likely cease, with other tenors set to remain in place until 2023.
- We expect a degree of ongoing uncertainty around whether and how the FCA will use its new powers to change the LIBOR methodology to facilitate the resolution of tough legacy products, though clarification may follow in H2.
- We expect EURIBOR to remain in place in the medium term, though industry will nevertheless need to incorporate fallbacks into contracts for EURIBOR to the same extent as for other IBORs.
- Conduct risk will remain high on the supervisory agenda, and firms will be challenged regularly and robustly on the steps they are taking to manage these throughout the transition.

Banks look set to be ready to complete the transition, given the supervisory scrutiny to which they have been subject over the last few years. But the wider market – corporates, insurers and some investment managers – remain less engaged in comparison. Within the corporate sector, and particularly among SMEs, awareness is generally lower, with many businesses also understandably preoccupied with their pandemic responses. However, if the lending market in certain RFRs does not increase in the first half of 2021, there will be an increased risk of a disorderly transition. If negative rates are introduced in the UK, this may complicate the transition, requiring additional client outreach and reviews of

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Final call for IBOR

contracts and systems, some of which may cut across similar work already done to prepare for IBOR transition.

LIBOR will survive beyond the end of 2021 in some form to cover 'tough legacy' contracts, with the real question being in which currencies and tenors, and how its calculation may change. With the administrator of LIBOR, IBA, intending to cease publication of the majority of LIBORs – including some tenors of USD – at the end of 2021, it is now largely a matter for the FCA to decide where it will deploy its new powers to allow the remaining LIBORs to persist beyond the end of the year. At a minimum, EUR and CHF LIBOR look set to disappear entirely, while some tenors of GBP (most likely one, three, and six months) and JPY are likely to stay. One week and two month USD LIBOR will also cease by the end of 2021, although other tenors may remain in place until the middle of 2023 to allow legacy contracts to mature. It remains to be seen whether the FCA will declare the remaining LIBOR currency-tenor pairs 'unrepresentative' after the end of 2021, and their form therefore also remains uncertain, as they may remain in place under different methodological approaches. However, we do not anticipate an early statement of intent from the FCA around specific methodological changes while it continues to explore available options. Firms can nevertheless expect supervisory pressure to cease issuance of new LIBOR-linked products over the course of the year, with US authorities in particular indicating that entering into USD LIBOR contracts after the end of the year 'would create safety and soundness risks'. Indeed, these issues will be present for all currency-tenor pairs that survive beyond end-2021.

In the meantime, supervisory pressure will focus on shrinking the pool of LIBOR-linked contracts to what HM Treasury has referred to as an 'irreducible core', and the FCA as a 'narrow pool'; indeed, the FCA has warned that firms waiting for regulatory action to amend the LIBOR methodology 'will not have control over the economic terms of that action', and that this may not deliver customers' 'preferred outcomes'. Firms that wait for the FCA to act run the risk of supervisory action further down the line if they are unable to demonstrate that their rump of tough legacy is as small as possible, especially if this results in sub-optimal outcomes for clients. Industry will also need to be ready for the possibility that methodology changes create additional basis risk to be managed. The most challenging legacy products will be exotic, non-linear, OTC derivatives, syndicated debt, certain varieties of floating rate notes, and preferred stock issuances.

The ISDA fallbacks protocol will lay the groundwork for the removal of IBORs when it becomes effective on 21 January, although banks in particular will still have to work hard to secure widespread client buy-in. The availability of the fallbacks protocol will not assist in the transition of tough legacy products, but we nevertheless see uptake of the protocol as a key indicator of the general readiness for transition in the market. Banks also need to ensure that they are operationally prepared to deal with the fallbacks in terms of their systems and processes, for instance end-to-end in their booking models. For the cash market, there remains no equivalent solution, and there will still be a need for bilateral negotiations to resolve contractual issues relating to the transition. Furthermore,

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

it appears increasingly clear that in some jurisdictions (notably the US) we will see continuing work to develop 'alternatives to the alternative', suggesting a lack of private sector alignment to any single alternative rate.

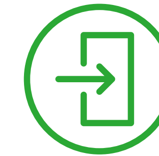
EURIBOR presents a somewhat different story. We do not see EURIBOR disappearing soon, with ESMA having emphasised its intention to maintain it in its revised form. But this does not obviate the need to introduce fallbacks into contracts, with the ECB having reiterated the need for banks to 'be prepared for all scenarios'. The continuation of EURIBOR may also create an interesting challenge with respect to €STR, given that firms with significant EURIBOR contracts may prefer to transition EUR LIBOR contracts to EURIBOR over €STR, which in turn may have implications for €STR liquidity.

While supervisors have been relatively more focused on banking, the insurance and investment management sectors continue to be exposed to numerous transition risks of their own. For life insurers this comes from the Solvency II RFR term structures, while non-life firms face similar challenges to corporates in terms of their exposures to the transition via IBOR-referenced contracts. Insurers should understand their exposures, perform stress tests to assess worst-case scenarios, and engage with EIOPA and the PRA as they work towards industry-wide solutions for the RFR term structures, recognising that discounting will need to start transitioning to new RFR term structures in 2021. Asset managers are considerable users of IBOR, and over the coming months asset managers should discuss with customers, regulators and benchmark administrators their plans to move away from IBOR and how this will affect any funds which are measured against an IBOR-related benchmark.

The FCA has been consistent and robust in its focus on FS firms', and in particular, banks', management of conduct risks, and they can expect supervisors to require ongoing evidence of the steps they are taking to manage these risks. Conduct risk is also highly pertinent for asset managers, some of which have less mature approaches to conduct risk management than the banking sector, making it all the more important that they give these issues the attention they need and are clear with end investors on the effect transition may have on the fund and its performance. There is a significant information asymmetry between FS firms and their clients on transition issues, making client communications around reference rate changes particularly important. Firms must provide customers with clarity on which rates are being changed and when, and ensure that these messages are delivered in an accessible and consistent way to different customer groups. And while banks continue to progress products on new RFRs through product approval processes, challenges remain. Firms in particular need to ensure they are systematically comparing the new rates to LIBOR throughout the transition in order to avoid inadvertently providing customers with worse rates than they would have received on a LIBOR contract, with a risk of action if customers lose out. The FCA recently reiterated this point, along with the message that firms 'will need to be able to demonstrate' how their approaches to transitioning customers are 'fair to the customer'.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Brexit – beyond the transition period



Overview

As expected, the provisions in the UK-EU TCA had little to say about cross-border financial services. Nevertheless, the fact that there is an FTA is positive for the business environment in which the FS sector operates and its customers. With the transition period having ended, banks will continue to deliver on the substance agreed in their EU authorisation plans and begin ironing out some of the inefficiencies created by their new operating and business model. We anticipate increased EU supervisory pressure for certain clearing activity to migrate to the bloc. FS firms will also follow closely data protection developments, particularly the data adequacy process. While we regard a positive decision on the UK's data protection standards as likely, it is not a foregone conclusion. Finally, delegation is set to be a hot topic for asset managers in both the UK and EU.

In focus

- We expect banks to deliver on the substance agreed with regulators as part of their transition plans. We also expect more banks to begin thinking about their post-relocation optimisation transformation projects, driven by the business need to optimise EMEA operations.
- We expect increased EU regulatory and supervisory pressure for certain UK clearing activity to migrate to the EU, even in advance of formal regulatory equivalence decisions.
- A positive data adequacy decision is now quite likely in our view, but still not a foregone conclusion. Firms should continue to prepare for continued uncertainty and different possible outcomes.
- We expect delegation to be a contentious issue for asset managers in the year ahead.

Banks' authorisation plans

The last several years have seen banks establishing or expanding entities in the EU, to ensure continued access to EU markets and meet ECB supervisory expectations [Figure 9 and 10]. The pandemic may have hindered some employee relocation plans, but we do not expect supervisors to give firms any leeway in terms of moving the assets and substance agreed in their authorisation plans, in line with the ECB's recent communications.

Though progress on the Capital Markets Union has been slow, we expect banks to reflect on their post-relocation transformation, driven primarily by the business need to optimise their presence across EMEA as a whole. Brexit projects have in many cases introduced (or increased) operational, capital and liquidity

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Brexit – beyond the transition period

Figure 9 – banks' asset relocations from UK to the euro area

Figure 10 – banks' asset relocations from UK branches to France

inefficiencies through duplication; with the macroeconomic environment remaining challenging, firms will be looking to address inefficiencies promptly. The search for efficiency gains in market risk and capital allocation across entities, and in outsourcing arrangements, will be key in firms' post-relocation optimisation transformations.

In planning and executing optimisation plans, we see four distinct regulatory considerations for banks. First, banks will need to consider the IPU requirements taking effect in the EU at the end of 2023, and the IFR/IFD, which in 2021 will require certain investment firms to reauthorise as credit institutions. Second, while the Commission has made clear that it will not assess equivalence in relation to the cross-border provision of investment services in the 'short to medium term', it has not ruled out equivalence related to the derivatives trading obligation and the share trading obligation, both of which have implications for where trades can take place and market liquidity.

Third, conclusions from the EBA's report on the treatment of third country branches, expected in Q2 2021, will be a leading indicator of the EU's appetite for and attitude towards such branches. Finally, UK-EU regulatory divergence – and its knock-on effects on equivalence being granted, or, where granted, maintained - will be relevant as firms look at their geographical footprint in the medium term. The more fragile the foundation for equivalence is, the less banks will be inclined to rely on it in the medium term and the more substance they are likely to shift to the EU. Here, firms await the UK-EU Memorandum of Understanding on cooperation, scheduled to be agreed by March 2021, which is expected to consider the equivalence process.

CCPs

The Commission's time-limited equivalence decision for the UK's regime in relation to CCPs dealt with the end-2020 cliff-edge risk, while introducing a new one at 30 June 2022. The Commission made clear that it expects market participants to use this breathing space to reduce exposures to UK CCPs,[29] and we expect increasing EU supervisory pressure for certain clearing activity – notably in EUR and EU

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

currency denominated derivatives - to migrate to the EU. In the absence of such pressure, business will not migrate of its own accord. We also anticipate EU CCPs to expand their clearing capabilities and incentivise market participants to conduct increased clearing activity in the EU. Whether these combined efforts will make significant inroads into UK CCPs' dominant market share of European clearing activity over the next 18 months is not yet clear. Ultimately, if the EU does not see the desired reduction in EU exposure to UK CCPs, ESMA's medium-term assessment of the systemic importance of UK CCPs, expected before the end of June 2022, could deny recognition to a UK CCP, or to some of its clearing services or activities.

Data flows

The EU has agreed to allow personal data flows from the EU to the UK to continue unchanged for up to six months from 1 January 2021, provided the UK makes no changes to its data protection regime during this period. This temporary provision should give the Commission time to complete its adequacy assessment. A positive data adequacy decision is now quite likely in our view, but still not a foregone conclusion. Firms should continue to prepare for continued uncertainty and different possible outcomes. If adequacy is not granted, or is but is subsequently revoked because the UK data protection regime diverges in substance from the EU's, firms will need to implement additional safeguard measures to transfer personal data from the EU to the UK.

Most FS firms will already have implemented changes to ensure continued data sharing between the EU and UK at the end of the transition period in the absence of an adequacy decision. However, the appropriateness of the alternative transfer mechanisms firms may have employed has recently been called into question by a CJEU ruling (Schrems II) which also invalidated the Privacy Shield for EU/US data transfers. Firms should assess data transfers and whether supplementary measures are needed in line with the EDPB's recent guidance[30] and the Commission's new SCCs.[31] Firms' business models and innovation strategies rely on unencumbered international data transfers, and firms will need to follow UK-EU data protection developments and ensure contingency plans are in place to respond to different possible outcomes.

Delegation

Delegation of portfolio management by EU-based asset managers to entities located in third countries, which is fundamental to current business models, will be firmly in the spotlight in 2021. The Commission's consultation on the AIFMD review[32] notably poses questions around whether delegation rules should be complemented with quantitative criteria or a list of core functions that cannot be delegated. The UK manages £2.1 trillion of funds delegated from Europe,[33] and this issue is therefore critical for UK-based asset managers managing portfolios on behalf of EU affiliates or clients. The CBI's warning to Irish asset managers to fix 'serious shortcomings' in the governance of delegated activities in their Irish entities is further grist to the mill for those who would curb delegation. Firms will therefore need to ensure that controls over delegation are sufficiently robust. While changes to delegation are not yet a 'done deal', and nor will firms taking this action ultimately guarantee the avoidance of significant restrictions, evidence of ineffective controls will only increase the probability of delegation rules tightening significantly.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Sustainability

Overview

Regulatory work on sustainability has continued as a consistent priority throughout the pandemic, reflecting the supervisory determination that firms should assess and disclose the extent of their exposures and manage them appropriately. The EU has continued to progress its ambitious sustainable finance action plan (with a renewed sustainable finance strategy expected in Q1), which the UK will seek to match in substance if not exactly in the same form. COP26 will focus attention on the need to deliver tangible progress on initiatives and new proposals to facilitate the flow of finance in more sustainable directions. Regulators continue to progress various climate-related stress test initiatives, while at the same time pressing firms to integrate ESG considerations fully into their risk management frameworks and business strategies. Meanwhile, we expect regulators and firms alike to prioritise finding a solution for the issues around ESG data and methodologies, and for regulators to pay increasing attention to climate-related conduct risk and market disclosure.

In focus

- Lessons learned from the results of climate-related scenario analysis and stress tests will highlight how far stress testing capabilities and data need to develop, and the need for corporate strategy and risk management planning to become better joined up. In response, supervisors will ask firms to accelerate their plans for developing climate risk management capabilities.
- The focus of banking supervisors on embedding ESG factors within the ICAAP and SREP means that by end-2021 climate risk will increasingly be a 'business as usual' determinant of regulatory capital costs for banks, with insurers likely to follow.
- We expect to see the development of industry-led ESG data sharing solutions, building on existing regulation such as the EU's Taxonomy.
- Climate change raises a number of conduct-related risks for firms, with market data and 'greenwashing'[34] expected to be key focus areas for supervisors.

Climate-related financial risk management and capital

In Europe, banks (and, in the case of the UK, also insurers) face two immediate deadlines. The ECB's Guide on climate-related and environmental risks took effect from 2020[35] and the UK's PRA expects banks and insurers to have fully incorporated climate-related risks into their overall risk management frameworks by the end of 2021.[36] Banks subject to the ECB's Guide will undertake a self-assessment exercise in early 2021 as mandated by the ECB, and we expect many will find significant gaps in their current practices relative to the ECB's expectations. 2021 will therefore mark the start of significant remediation activities in advance of the ECB's full supervisory review

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

planned for 2022. UK banks and insurers will similarly find it challenging to meet fully the PRA's expectations. Supervisors understand the constraints on what firms can achieve in the near term, but their expectations will also evolve as the 'art of the possible' develops. The capabilities that firms develop in the near term and their plans for future work should anticipate – in their design and implementation – this evolution.

Supervisors will continue to focus on climate scenario analysis and stress testing. In the UK, the focus from June will be on the BoE's ambitious CBES, in which the largest banks and insurers have been invited to participate. Elsewhere, France's ACPR launched a voluntary climate-focused pilot exercise in June 2020, with results due to be published in April 2021, and a methodology assessment to identify key lessons learned to follow.[37] The ECB will publish details of its 2022 climate-related supervisory stress test in 2021,[38] which we expect to be aligned to ongoing work by the EBA to develop a dedicated climate change stress test. These will highlight shortcomings in firms' capabilities and spur supervisors to set expectations to accelerate the pace of development. Moreover, the NGFS, and the UK Government as host of COP 26, are encouraging the adoption of climate-related scenario analysis and stress testing, and firms should be prepared for more stress tests of this kind as more supervisors introduce exercises.

In last year's *Regulatory Outlook*, we noted the emerging debate about the use of green incentivising and brown penalising factors in the bank and insurance capital frameworks. Although the European Parliament is due to discuss capital charges for climate-related risks, we do not expect anything tangible to emerge in 2021. Supervisors are, however, clear that banks and insurers should already be considering to what extent climate-related risks in turn affect existing risk considerations - e.g. for credit, market, operational or liquidity risk, and therefore the capital required to be held against those risks. The EBA's discussion paper on management and supervision of ESG risks proposes how these factors can be incorporated into the supervisory framework. The BoE has indicated that it will similarly develop its own approach in the coming year. Though banking supervisors seem to be moving forward more quickly, in our view, any tangible development of this approach will also extend to insurers. This means that banks and insurers will have to show progress in terms of how they allocate capital for climate-related risks (although the EBA, for example, has also said that it does not expect to see across-the-board capital requirements for banks reflecting this risk). Similarly, we expect supervisors to ask firms for evidence of how they are incorporating climate risk into their risk appetite statements, not only qualitatively but increasingly quantitatively.

'Supervisors will continue to focus on climate scenario analysis and stress testing.'

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Sustainability

Though we do not expect significant divergence between the UK and EU's respective approaches to climate-related regulation, internationally active FS groups may find it increasingly challenging to develop a consistent group-wide framework for sustainability. This is largely because while regulators broadly agree on the outcomes they expect FS firms to achieve, their approaches to achieving those may differ (including within Europe) and the speed at which they are proceeding is quite varied, with Europe generally moving much quicker than other regulators within EMEA and globally.

ESG data and taxonomies

In the near term, the most challenging area for all FS firms is likely to be in relation to ESG data and methodologies. There is a superabundance of climate ratings but a scarcity of relevant, comparable and reliable data. Firms need to invest time and resources in 2021 to develop systems and approaches to gather and organise data, whether relying on external providers or performing in-house analysis, to ensure appropriate due diligence on investments, counterparties or customers.

Companies will have to establish their own data origination approaches. We expect to see industry-led ESG data sharing solutions develop in 2021. In the UK, the Climate-related Financial Risk Forum is planning to explore what practical steps firms can take to address data challenges.

The investment management sector will continue to play a prominent role in developing indicators of ESG factors and availability of data, responding to mounting investor and regulatory pressure to disclose climate-related risks. Asset managers and advisers will also need to respond to a number of significant initiatives over the course of 2021, including the Disclosures and Taxonomy Regulations and the EU Delegated Acts amending UCITS, AIFMD and MiFID II. To respond effectively, they will have to address a number of challenges, not only as they pertain to data but also in relation to understanding the scope of the new regulations and making sure they have the relevant expertise. Industry-driven initiatives to set out taxonomies for other sectors will build on what regulators have done for investment management.

Conduct risks

Climate change raises a number of conduct-related risks, with market data and 'greenwashing' of particular concern for supervisors. These risks may also present liability risk to firms, in the event that the firm, or a counterparty, is subject to litigation due to greenwashing or disclosure failures. Firms must provide the market with reliable and sufficient information about their material exposures to climate change in line with regulatory requirements. A review of the NFRD is expected in Q1. In terms of products and services, action by policymakers to channel funding to sustainable investments provides firms with opportunities in relation to 'green' products. However, conduct risks that might arise are still relatively unexplored.[39]

Within the investment management industry, to counter any perception of greenwashing, firms will need to review their processes for conducting due diligence on investee companies and other financial products, for matching green products to clients based on their requirements, and, in the case of an in-house product range, for marketing. Although

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Sustainability

regulators' concerns are likely to centre on mis-representation, intentional or otherwise, there is the potential for inadvertent greenwashing if there is insufficient data about investee companies to provide an accurate picture to clients. As sustainable investing becomes more mainstream, the FCA and other regulators will have more evidence on consumer outcomes and hence where the prevalence of greenwashing is concentrated, and are likely to tackle such issues as they become apparent.

Banks and insurers will need to ensure that their 'green' product offering is aligned to their climate change strategy. Issuing, underwriting, distributing, or investing in 'green' products will require robust control frameworks for valuation, modelling, accounting, due diligence, product governance, and disclosure.

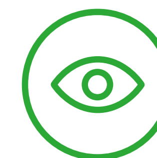
Country spotlight: South Africa – a nation at the beginning of its sustainability journey

South Africa is at the beginning of its journey away from fossil fuel dependency. Notwithstanding this, it is leading the way in sustainability-related regulation and guidance for firms in the region. Regulators, policymakers and central bankers are starting to think about ways to facilitate the transition to a greener future by encouraging the financial sector to act sustainably. For example, the SARB recognised in its May 2020 financial stability report that climate change poses a risk to financial stability, and that enhanced disclosures and new approaches to modelling climate risk are required. In 2021, we are likely to see a greater regulatory push to close some of the gaps in relation to sustainable finance regulation in South Africa, including for example developing a benchmark climate risk scenario for use in stress tests, incorporating voluntary codes of principles into regulatory regimes and developing or adopting a taxonomy, consistent with international developments.

Though the regulatory framework is still developing, there is already significant investor pressure on South African firms to integrate ESG factors into core areas of their business. This is particularly the case with social factors, which historically have been prioritised over environmental concerns. Over the next year, South African firms will have to give further consideration to environmental factors, in particular how these interact with their social agenda, implementing more outcomes-based investment strategies and reporting systems that consider these issues in parallel. As in many other African countries, in South Africa, the traditional energy industry driven by fossil fuels is a significant source of employment while also a driver of economic activity. Therefore, the socio-economic impact of any climate-related commitments is going to be contentious, with a difficult policy and regulatory road to balance these factors ahead.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Conduct, culture and governance



Overview

Conduct risks are inherent in industry responses to COVID-19, putting a premium on firms' cultures and quality of governance. Supervisors will look for evidence of cultures that, both in principle and in practice, deliver good customer outcomes and recognise wider social expectations. Firms simultaneously face pressure to manage their financial resilience, creating tensions between conduct and prudential obligations; these will crystallise most prominently in lending and forbearance decisions, and in collection and recovery processes. The regulatory spotlight will fall on firms' treatment of customers whose situations are not clear-cut and for whom the right outcomes are therefore less certain. Regulators will also monitor the recent growth of 'credit-like' products, and take action if they uncover evidence of consumer harm.

In focus

- As firms navigate the continued uncertainty created by COVID-19, there will be renewed supervisory assessment of their culture from a customer outcomes and wider social perspective, and, in that light, of the quality of their governance and risk management oversight.
- 2021 will see growing tension between firms', especially banks', conduct and prudential obligations as they attempt to balance achieving fair, flexible outcomes for customers in financial distress (both retail and SME) with the need to avoid a deterioration in asset quality and a build-up of NPLs.
- As COVID-19 has accelerated the presence of alternative 'credit-like' products (e.g. BNPL products), we expect regulators to consider stronger regulatory requirements including bringing these products within their regulatory perimeter if there is evidence of harm to customers.

COVID-19 and vulnerable customers

As system-wide temporary payment breaks come to an end and financial distress increases, conduct regulators will work to ensure fair outcomes for customers. Research suggests that there are 12 million people in the UK with low financial resilience and who may struggle with bills or loan repayments [Figure 11].

At the same time, prudential regulators emphasise that lenders must manage their financial resources responsibly, minimising any deterioration in asset quality or a build-up of NPLs.[40] Supervisors are mindful that short-term forbearance could well understate the scale of problem debt, as well as potentially leading to poorer longer-term outcomes for customers. Firms will be expected to engage

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Conduct, culture and governance

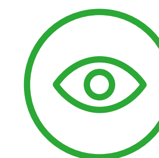


Figure 11 – FCA survey data highlights magnitude of consumers likely to struggle with debt due to COVID-19[41]

proactively with borrowers before payment breaks end to assess repayment capacity. Whilst giving customers sufficient time and support to recover financially, additional forbearance should be sustainable and tailored. Mindful of historical episodes regarding the poor treatment of SME businesses, supervisors will also expect these customers to be treated fairly.

For lenders, forbearance decisions will require finely balanced and case specific judgements, particularly where borrowers' financial situations are uncertain. Lending and forbearance decisions, and the treatment of customers through collections and recovery, will attract intense supervisory scrutiny; conduct supervisors will be sceptical of 'one-size-fits-all' approaches. Lenders will need to leverage data and analytics to inform decision-making and monitor whether products and solutions remain appropriate given customers' changing circumstances, bearing in mind their regulatory obligations in this regard. Demonstrating fair customer outcomes, and ensuring that boards and senior management have appropriate oversight, will require enhanced reporting and MI, including quality assurance and customer outcomes testing.

Tension between conduct and prudential obligations and commerciality will play out in the insurance sector through legal cases (such as the UK business interruption insurance test case). Here, insurers may be exposed to prudential risk through claims for which they have not priced or reserved; conduct obligations or the threat of reputational damage may both create pressure to pay.

Increased co-ordination between conduct and prudential supervisors would be beneficial, but the pandemic could create fault lines, particularly in twin-peaks regimes such as the UK and South Africa.

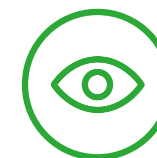
COVID-19 has also accelerated the growth of alternative 'credit-like' products (e.g. BNPL type products), to which supervisors will remain alert. In Sweden, this has, in part, prompted new regulations to discourage online shoppers from paying with credit whilst the UK's FCA is undertaking further research into the sector. If it finds evidence of customer harm, we expect a push for these products to be brought within its regulatory perimeter. To prepare for potential regulatory intervention, firms providing such products should therefore review them against likely regulatory expectations, identifying any gaps.

Culture and governance

COVID-19 has expanded the ranks of vulnerable customers, creating a major test for culture and governance across the industry. Regulators will re-emphasise the importance of what the UK's FCA has referred to as

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

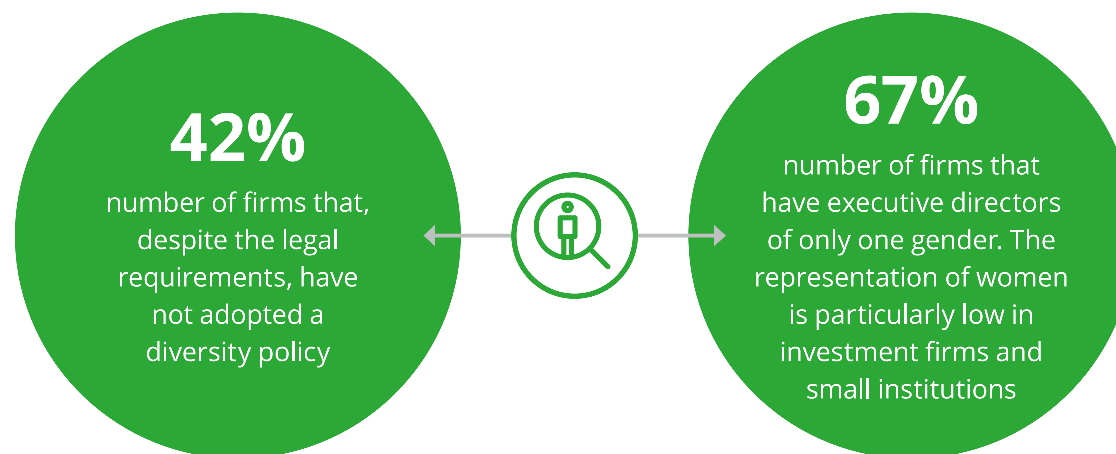
Conduct, culture and governance



'purposeful' cultures as a means of helping firms respond to the varying challenging circumstances faced by their customers. Supervisors will judge evidence of poor treatment of customers as a de facto failure of a firm's culture and governance, justifying a robust response.

Supervisors also expect firms to make meaningful progress towards more diverse and inclusive cultures as a way of improving decision-taking and mitigating the risk of 'group-think'. This will be particularly important for firms supporting decision-making through AI. Ensuring equal opportunity is occurring in recruitment, promotion, and especially board and senior management appointments and succession plans, will attract increased regulatory priority [Figure 12]. We also expect a growing emphasis on increased ethnic minority representation as a result of the broader focus on social justice prompted by the events of 2020. Firms at the start of their diversity journey will need to establish and embed diversity policies, while all firms will need to demonstrate how they will sustain diversity initiatives and avoid 'tokenism'.

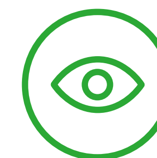
Figure 12 – EBA 2020 report (based on 2018 data) shows firms' shortcomings across Europe in relation to diversity[42]



Supervisors are increasingly determined to ensure that senior management take responsibility for their actions, including in countries without formal accountability regimes. Regulatory and supervisory focus on individual accountability will continue to grow, with the ECB intending to strengthen its fit and proper guidance and ensure that directors deemed responsible for misconduct (or for failing to challenge the misconduct of colleagues) 'will no longer be able to hide behind the collective responsibility of the board'.[43] Boards and senior managers will need to ensure that they operate within the spirit as well as the letter of regulation. This will include ensuring that their decisions achieve demonstrably fair outcomes for customers and employees, and that there are robust controls in place to monitor these.

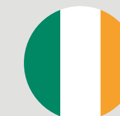
Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Conduct, culture and governance



Country spotlight: Ireland – a pacesetter in supporting vulnerable customers

Ireland has had a framework and rules in place prescribing the manner in which vulnerable customers are identified and managed since 2012, years ahead of some of its European peers. While prescribed rules go a long way in informing a framework for firms to ensure appropriate protection for vulnerable customers, the CBI has been a change agent in progressing the meaning - and interpretation - of vulnerabilities in new areas.



Financial vulnerability	During the Tracker Mortgage Examination in Ireland which saw around 40,100 customers affected by tracker mortgage failings by affected firms, the CBI held providers to a higher standard in the protection of those individuals who were financially vulnerable. This cohort of customers was treated as a high-risk vulnerability class that warranted a higher degree of protection.
Digital vulnerability	With the increased drive towards digitised business models, the CBI encourages firms to ensure the needs of existing customers, including those who may be digitally vulnerable, continue to be met. In particular, firms must ensure that cohorts of customers are not financially excluded by virtue of customer journey design.
Wellness/age-related vulnerability	Instigated by the pandemic's impact on swathes of individuals suffering financial difficulty due to illness, the CBI has encouraged firms to engage sympathetically and positively with customers to support them through difficult periods. Additionally, the CBI has encouraged firms to help customers who are isolating to manage their banking in a safe, alternative manner.
Market volatility vulnerability	Lastly, the CBI paid special attention to retail investors who may be vulnerable to greater market volatility and uncertainty through COVID-19. It guided firms to monitor and evaluate products sold during this turbulent period to retail investors to take account of vulnerabilities as a result of COVID-19.

Nuanced failings by firms in Ireland through the Tracker Mortgage Examination and other events gave rise to an evolved interpretation of the meaning of customer vulnerability, which the CBI has applied through COVID-19. We expect a continued expansion of the definition of customer vulnerability and more regulatory pressure on firms to develop long-term approaches to deal with customers experiencing hardship or social exclusion as a result of the pandemic. The regulatory spotlight will fall on firms' processes for identifying vulnerable customers, and the associated actions that firms should take. In 2021, as the CBI finalises its substantial review of the Consumer Protection Code, we may see further guidance in relation to its expectations around the treatment – and definition – of vulnerable customers.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Deploying digitisation and innovation

Overview

Consumers' use of digital financial services has increased significantly due to COVID-19, most notably for payments [Figure 13]. Digitisation and technological innovation in FS will be key to economic recovery and growth, and digital consumer habits formed through the pandemic are here to stay. Implementation of the EU and UK's ambitious digital strategies will begin in 2021, and FS firms have an opportunity to shape a more innovative and competitive regulatory framework. Industry must also be sensitive to the supervisory concerns raised by the speed and urgency of digitisation, including on the Cloud, operational resilience, conduct risks in payments, and the use of AI and big data analytics. Regulators and supervisors are also pressing ahead with enhancing their own data and technological capabilities, which will shape the future of supervisory engagement.

In focus

- Firms will need to revisit business critical Cloud migrations completed apace in 2020 to make sure all necessary controls are in place. We also expect firms, meanwhile, to resume – and in some cases accelerate – strategic medium-term migrations.
- Firms' use of data and AI will increase in light of COVID-19, and we expect an increasing focus from supervisors to ensure that firms' use of AI is compliant, ethical and robust.
- Supervisors will increase their scrutiny of payment firms' and e-money providers' practices in relation to safeguarding of customers' funds, business continuity and wind-down plans, and management of outsourcing risk.
- Regulators and supervisors will press ahead with enhancing their own capabilities and teams in relation to their use of SupTech. We expect use cases, including market abuse monitoring and digital reporting, to gain speed in 2021.

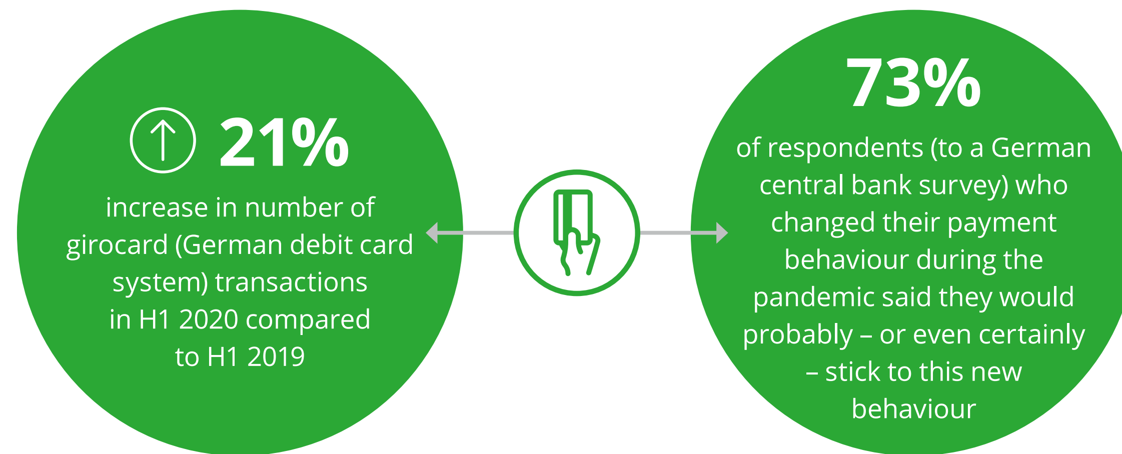
Digitisation plans and the Cloud

To respond to new ways of working, reduced face-to-face customer contact, and cost pressures, firms with the capacity to do so should press ahead with comprehensive digitisation programmes. Those with more limited resources should consider alternative ways forward, either by specialising or partnering with other firms for example. Indeed, 95% of European respondents to a recent Deloitte FS survey are already implementing or planning to implement accelerated digital transformation of business services. In 2021, firms' tactical responses to COVID-19 should lead to more strategic thinking about the effectiveness, robustness and resilience of digital operations, including their increasing reliance on a remote workforce and TPPs.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Deploying digitisation and innovation

Figure 13 – will COVID-19-related trends in payments remain in the medium to long term?[44]



Cloud migration will underpin firms' digitisation programmes. While Cloud-based business models performed robustly through COVID-19, we do not expect this to diminish regulatory scrutiny of migration plans. At the outset of the pandemic many firms prioritised business critical Cloud migration projects, for example those enabling remote working. Supervisors remain alert to the pace at which some of these projects were completed, and we expect them to press firms in 2021 to revisit these arrangements and ensure the necessary controls are in place, and apply lessons learned in their medium-term Cloud plans. Firms should review implemented architectures and controls, identify and address any shortcomings, and validate their adherence to internal governance arrangements.

We also expect firms to resume, and in some cases accelerate, their strategic medium-term Cloud projects in 2021. Firms should engage as early as possible with supervisors, well in advance of any key decisions, giving them time to build in supervisory considerations. Supervisory engagement should cover both technical risk and the governance aspects of the migration, as well as budget and timeline. As regulators around Europe increasingly move their own activities onto the Cloud, firms should expect regulators' questions to become more pointed as they gain more direct experience in Cloud migration.

Outsourcing to CSPs has been under the regulatory spotlight because of concerns around concentration risk, single points of failure and vendor lock-in. As they continue to innovate, it would be wise for firms to ask themselves which of their other service providers - for example payments or AI technology or data providers - share some of these characteristics or introduce additional fourth-party outsourcing dependencies. If these providers are likely to become critical to providing important business services, the regulatory attention currently on CSPs may extend to these technology providers. Firms can act proactively and ensure their innovation and outsourcing plans will stand up to scrutiny,

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Deploying digitisation and innovation

once full-scale deployment and future growth are factored in.

Artificial Intelligence

Customers' demand for digital services, the pressure to reduce costs, and the need to boost operational efficiencies mean that firms' use of big data analytics and AI is expected to increase [Figure 14]. But regulators and supervisors remain alert to the risks. COVID-19 is also exposing some specific challenges in firms' AI governance and risk management. For example, the BoE recently confirmed that, as we highlighted previously, the pandemic has had a negative impact on the performance of some ML models.[46] The sudden changes in consumers' behaviour and economic conditions caused by the pandemic led to unexpected model drift, i.e. the data used to build ML models and their statistical properties are no longer sufficiently relevant to predict future outcomes as reliably as before.[47]

Figure 14 – will the pandemic increase FS firms' use of machine learning?[45]

25%

proportion of the largest UK financial firms with increased plans to invest in machine learning

In 2021 we expect a continued focus on ensuring that deployment of AI is rooted in regulatory compliance, complemented with strong ethical frameworks to help fulfil supervisory, customer, and social expectations. In the UK, we expect regulators to focus on explainability and transparency. As the BoE survey highlights, COVID-19 has had a negative impact on the performance of some ML models. This is linked to the fact that ML models' performance can change or deteriorate under conditions different to those displayed in the data on which they were originally trained. This can occur either when the underlying data changes (data drift) or the statistical properties of the data change (concept drift).

The pandemic has led to both data and concept drift, which has challenged models in unusual and unexpected ways. Therefore, monitoring for data drift and concept drift is one of the key challenges for firms to ensure appropriate risk management.

With some requirements intersecting significantly, firms should take a holistic approach to data protection, conduct regulation and ethics to ensure good customer outcomes, compliance and operational efficiency. Effective AI risk appetite and ethical frameworks are necessary, but specific risks, potential harms, and ethical considerations will need to be understood and addressed in the context of each AI use case. Engaging with consumers and civil society organisations in both the design and testing of AI systems will help firms understand and fulfil society's ethical expectations. Regulatory engagement on AI risk mitigation plans can help firms resolve context-specific compliance challenges. Regulatory sandboxes (where available) are useful in terms of giving firms the confidence to innovate; vulnerable customers, fraud, and SME lending are focus areas for the FCA's Digital Sandbox pilot, for instance. Firms should also collaborate

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Deploying digitisation and innovation

on specific use cases (e.g. financial crime) to voice challenges that could benefit from further regulatory engagement or guidance, and develop leading practice to address regulatory and data protection issues.

Payments

The payments sector has experienced widespread changes in recent years, spurred on by initiatives such as PSD2 and Open Banking, and the shift to digital payments in light of COVID-19 adds momentum to this change. The ambitious payments strategies launched at the EU[48] and UK[49] level in the second half of 2020, as well as the FSB's work on cross-border payments,[50] speak to the long-term strategic significance of payments in the post-pandemic world. But the pandemic and recent failures have also highlighted the risks posed by the payment sector, including two important near-term issues that we expect to be front of mind for supervisors over the next year.

Figure 15 – payment companies at the core of the UK FinTech ecosystem[51]

First, there are weaknesses in how some payment firms and e-money providers safeguard customer funds and manage prudential risks, as well as their general governance and risk controls environment. In addition to large established firms, in the UK, the increasing number of small and medium-sized payment firms [Figure 15] could also collectively pose significant risks to the financial system in case of disorderly wind-downs. The pandemic has also increased the exposures of acquirers to chargebacks due to merchants that have failed, or will fail, before delivering products or services. The FCA is also alert to the potential for significant consumer harm where safeguarding shortcomings hinder repayment of customer claims.[52] Second, operational resilience risk in payment systems is increasing due to the complexity of the payments value chain and reliance on TPPs for critical regulated and unregulated activities. We expect supervisors to increase their scrutiny of payment firms' and e-money providers' compliance with existing rules and guidance.

In relation to customer funds, firms should prioritise addressing any shortcomings in relation to the identification and segregation of relevant funds, book-keeping, reconciliation and account administration; and monitoring and oversight. Firms should also consider commissioning independent reviews of safeguarding arrangements. They should develop a clear, board-approved management action plan to remediate any issues and ensure that robust policies, controls and documentation procedures are in place. Firms

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Deploying digitisation and innovation

should review systems and controls frameworks for their oversight of third parties and address gaps as necessary, updating business continuity plans to reflect any changes.

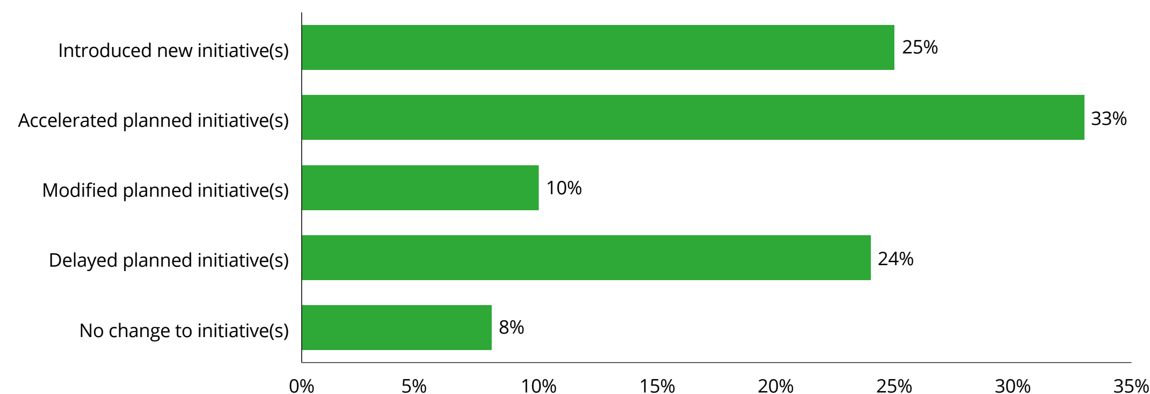
Payments and e-money firms should also expect intense scrutiny of their wind-down plans, which the FCA clarified are a condition of authorisation. Firms will have to put in place effective governance, risk appetite statements, and stress testing programmes to identify risks. Firms will also see a much greater supervisory focus on capital adequacy, which firms should assess on at least an annual basis, and liquidity. Finally, firms should be ready to evidence clearly how they could wind down the business in both a solvent or insolvent scenario.

RegTech and SupTech

COVID-19 has also accelerated and introduced new RegTech and SupTech initiatives worldwide [Figure 16]. In Europe, both the BoE and DNB, for example, have developed use cases in light of the pandemic.[53] In our view, the most promising SupTech use cases for 2021 include market abuse monitoring and digital regulatory reporting. SupTech will help regulators be more effective in their analysis and actions, and firms should keep abreast of developments to understand how best to prepare and respond.

Boards and senior management teams will be in an unenviable position if their supervisors are better able to detect risks in the data they report to them than they are themselves. As part of their digitisation plans, firms should consider the implications of SupTech deployment on their own risk and compliance management approaches, and the infrastructure necessary to connect with new technology-enabled supervisory processes. But we note that regulators will face the same risks as firms. For example, when validating and testing SupTech AI applications, regulators (like firms) should be alert to the challenge posed by COVID-19 in relation to 'model drift'.

Figure 16 – impact of COVID-19 on RegTech/SupTech initiatives by central banks and regulators[54]



Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Financial crime in the new normal

Overview

The mass shift to remote working has led to regulatory concerns that patterns of financial crime have been materially altered, and in some cases incentivised or facilitated. With regulatory patience in this area running thin before COVID-19, supervisors will likely accelerate initiatives to tackle financial crime in 2021. The immediate supervisory priority, however, will be to ensure firms maintain robust risk and control frameworks while working remotely. Firms should therefore enhance controls, and develop new tools to monitor, manage and report financial crime, leveraging all means at their disposal, including technology, as necessary.

In focus

- In 2021, as regulators push firms to enhance their AML/CTF capabilities and cost pressures continue, firms will be under increasing pressure to deploy additional measures to supplement transaction monitoring arrangements.
- Where there are supervisory concerns around market abuse or other financial crime activity, regulators will issue more detailed guidance around activities being undertaken from home. Supervisors will make more intensive and targeted use of accountability regimes, where these are in force.
- Regulators will increasingly endorse industry-driven data-sharing programmes in order to address concerns around higher levels of financial crime following the pandemic, by making the requirements to share personal data for the purposes of financial crime monitoring more explicit, giving firms a stronger lawful basis for processing personal data under GDPR.

Anti-money laundering and transaction monitoring

COVID-19 has added impetus to EU proposals to establish an authority responsible for AML supervision, due by March 2021,[55] and to facilitate cross-border cooperation between EU supervisors through AML/CTF-specific banking supervisory colleges. Guidelines for these colleges came into force in January 2020, but implementation will become more apparent this year. AML/CTF colleges will provide a permanent structure for supervisory information exchange to support more effective oversight of cross-border groups.[56] These structures will improve supervisors' view of the overall level of risk posed to banking groups operating in the EU, in turn facilitating co-ordinated supervisory responses. Banks with large European presences should prepare for enhanced cross-border AML/CTF scrutiny,

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

and stand ready to engage with NCAs within the college and respond to any resulting actions.

Near-term supervisory focus will be on enhancing firms' monitoring and identification of suspicious transactions, while encouraging the development of innovative and effective industry solutions to address shortcomings in relation to CDD and on-boarding. Two issues may pose challenges in this regard: the EU's data adequacy decision in respect of the UK, and lawful basis under GDPR. Though we regard a positive data adequacy decision as likely, unless and until there is one, flows of personal data between the EU and UK may become more challenging. Firms will need to put in place organisational, contractual and technical safeguards to ensure a similar level of protection for personal data transferred to the UK. If a positive data adequacy decision is not reached the UK and EU may consider entering into a specific data-sharing agreement on financial crime to overcome any issues. Second, regardless of whether a positive decision is reached, lawful basis under GDPR may continue to pose challenges to firms seeking to use innovative solutions for CDD and on-boarding in the absence of regulatory clarifications. But, we expect the market-wide reputational concerns, including from events such as the FINCEN leaks, and the current heightened level of risk, to drive regulators to support industry efforts by making the requirements to share personal data for the purposes of financial crime monitoring more explicit. This would give firms a stronger lawful basis for processing this personal data under GDPR.

In response to regulatory and cost pressures, firms should leverage innovative technology solutions to improve AML/CTF controls and transaction monitoring capabilities in 2021. They should also explore innovative ways of pooling data with others in the industry to achieve scale and identify uncharacteristic transactions patterns more effectively, while ensuring data protection risks are minimised through techniques such as pseudonymisation and federated learning.

Fraud

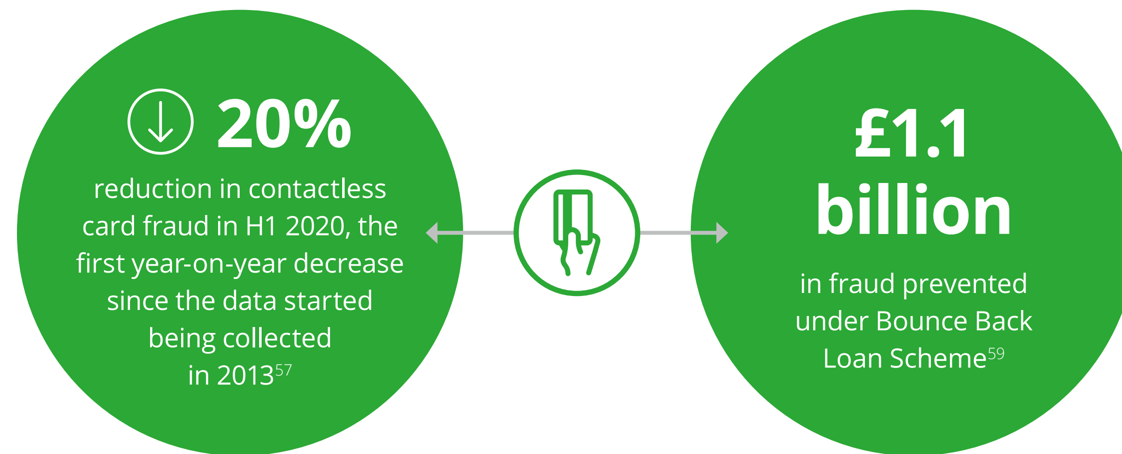
There has been an uptick in fraudulent activity throughout the pandemic, and supervisors have warned firms and consumers of COVID-19 scams. One area with considerable potential for fraud is government support schemes, given the priority attached when the schemes were first introduced to making the funds available quickly; UK lenders have declined £1.1 billion in potentially fraudulent Bounce Back Loan Scheme applications [Figure 17]. We expect supervisors to push firms to enhance their strategies to manage these evolving risks, and take action where controls are found to be lacking.

Firms should review and adjust controls as necessary, to reflect the increased level of risk. Investment firms in particular should communicate clearly risks around investment fraud on their websites and in other forms of communication. In the UK, banks that were not specifically directed by the PSR to implement 'Confirmation of Payee' scheme should consider doing so in any case to demonstrate to supervisors that the firm has taken reasonable steps to identify fraud or money laundering attempts.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Financial crime in the new normal

Figure 17 – Financial crime – COVID-19 has altered a range of patterns



Market abuse

Increased remote working, exacerbated by the scale and volatility of market activity, could also give rise to greater scope for market abuse and misconduct. Examples include control of inside information, e.g. where people working from home in the same household may have access to information they would not normally have, and a reduction in self-policing amongst office-based staff or fewer incidents reported to compliance teams given the diminished physical presence of the first line of control.[58]

Regulators will also be wary that market uncertainty and volatility are often accompanied by greater temptation to abuse the market.

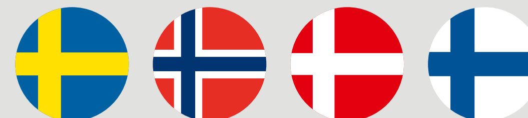
The UK's FCA has indicated an expectation that 'office and working from home arrangements should be equivalent',[60] while Germany's BaFIN expects firms to have market abuse monitoring systems and procedures 'even in changed working and market conditions'.[61] Where there are specific concerns, and if supervisors identify similar shortcomings across firms, this will lead to more specific expectations being articulated around activities being undertaken at home. In the UK this could mean using the SMCR to assign oversight of the remote working control environment to a Senior Management Function.

Firms should perform risk assessments; review and update compliance policies; provide staff with additional training; and adjust surveillance tools as well as making sure those that remain are GDPR-compliant, while ensuring that controls for inside information remain effective. In order to manage the increase in alert volumes, and challenges in dealing with backlogs and policy breaches, given the increased market activity, some firms have recalibrated or applied additional filters to their alert generation.[62] Where this is the case, changes to the calibration should be appropriately analysed, documented and governed. Firms should be under no illusion: supervisors are willing to collaborate in this area, recalling one significant 2020 instance of global supervisory co-operation that resulted in substantial penalties being levied on a firm.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Financial crime in the new normal

Regional spotlight: The Nordics – sharing data to tackle financial crime
Firms across EMEA interested in working with the wider industry to develop innovative ways to help tackle financial crime issues should take note of the Nordic experience.



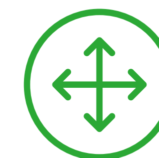
In 2019, the six largest Nordic banks founded 'Invidem' a shared utility that gathers and manages KYC information on corporate clients according to a pre-defined set of standards agreed to by the founding banks. Set to launch in 2021, it will combine the use of technology and third party vendor data to provide a KYC case file containing non-competitive information. This information is first shared with the corporate client – the owner of the data – who will be asked to verify the file, fill in missing data and subsequently grant permission to share its information with banks through the facility.

While the founding banks will be the first customers to use Invidem's services, they will also be open for purchase by other financial institutions affected by money laundering regulations. The desired end state is one where banks can access up-to-date KYC files for their corporate clients, and will receive a notification when, for example, there is a change in beneficial ownership. For banks, the utility will bring operational efficiencies, given reduced dependencies on vendors for similar services. The customer experience will also be improved through, for example, being able to share one file with multiple banks, reducing time spent dealing with multiple ad hoc KYC requests.

Firms across Europe will follow the initiative closely to heed any lessons for other similar initiatives. To this end, firms considering forming/taking part in similar initiatives should focus on agreeing data standards with fellow participants, while also allowing sufficient lead time to turn the utility into a reality.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

EU/UK regulatory divergence



Overview

The UK's departure from the EU provides an opportunity for UK legislators and regulators to revisit their implementation of a number of existing EU Directives and Regulations, at the same time as the UK's FS regulatory framework is poised to change. The sharp economic contraction in 2020 has placed renewed focus on economic growth, and the UK government may revisit key pieces of the UK's FS regulatory framework to enhance competitiveness and boost economic activity. In determining where to diverge, there are a number of competing factors to consider including the public perception of any reforms, the costs involved and financial stability considerations. In any case, the BoE will be keen to see it remains regarded as a standard bearer for robust prudential regulation as the UK adjusts to its new position post-transition period.

In focus

- We expect EU legislators to diverge – possibly significantly – from Basel 3.1 in order to reduce its impact on EU banks, particularly in light of the desire for banks to support growth as part of the post-COVID-19 recovery.
- We expect differences in the prudential framework between the EU and the UK to become increasingly stark, in terms of the timing of implementation and the substance and form of the rules they adopt.
- Material divergence between the UK and EU's implementation of Solvency II is likely. In the UK, we expect changes to areas including the Matching Adjustment while the EU looks more likely than the UK to retain a cost-of-capital based approach to the risk margin.
- In implementing its new IFPR, we expect the UK to take a different approach to the EU's IFR and IFD in areas including waivers to exempt firms from certain rules or requirements and how liquidity is considered for investment firms belonging to a larger group.

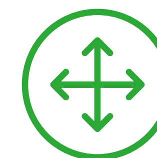
Banking and Capital Markets

Despite the UK's baseline strategy to 'onshore' EU FS legislation with equivalent requirements, areas of regulatory divergence – both in timing and substance – are likely to arise between the UK and EU. The UK's decision to implement Basel 3-related elements of CRR2 in January 2022 rather than the EU's 28 June 2021 is an early example.

EU legislators have considered trade-offs between strengthening banking sector resilience and supporting economic growth with each iteration of Basel rules, increasingly pointing to European specificities that might justify EU divergence from the BCBS standards. With the CRD6/CRR3 round of negotiations set to take place in an economic downturn, we expect EU legislators to diverge

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

EU/UK regulatory divergence



from Basel 3.1 in order to support banks' ability to fund the recovery. One likely area for divergence is the standardised output floor, which could see a longer implementation period, or the waiving of its applicability at sub-consolidated levels in banking groups. The so-called 'parallel stacks' approach, advocated by certain stakeholders in the EU, would likely widen divergence between UK and EU implementation if selected. The output floor will nevertheless introduce 'floor capacity' as a new measure in capital management, and in 2021 banks should put themselves on the front foot by considering how they will track and use floor capacity across their balance sheet. Another candidate for divergence is the standardised treatment of unrated corporates, as the capital impact of these revisions appears likely to hit EU banks much harder than their US counterparts, whose non-SME corporates are more likely to have a credit rating.

The implementation of prudential capital requirements in the UK will be largely regulatory-led rather than legislative, in contrast to the EU. This may lead to different priorities, with the technocratic process in the UK likely to prize adherence to international standards more than the political process in the EU. Although the PRA has a new mandate to consider economic growth and financial sector competitiveness in its adoption of BCBS standards,[63] we still expect the PRA to be more Basel-compliant than EU regulators in the adoption of Basel 3.1. An early indicator of this tendency is the PRA's position on the prudential treatment of software assets. In 2021 the PRA will consult on reverting to its previous policy of requiring banks to deduct the full value of software assets from their CET1 capital, effectively revoking a policy implemented in the EU at the end of 2020 with which the PRA has never been comfortable.

'We expect material UK divergence from the EU's implementation of Solvency II.'

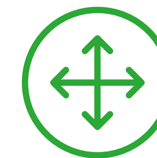
Insurance

We expect material UK divergence from the EU's implementation of Solvency II,[64] with the most profound change likely to be a shift to a more principles-based and judgement-based regime, closer in spirit and practice to the operation of the UK's former ICAS regime. We expect EU regulators, in contrast, to continue to align on areas of inconsistent application and judgment in Solvency II, necessarily leading to further codification of the EU regime.

The UK government has signalled clearly that it will reform the risk margin, with a move towards the less interest rate sensitive ICS approach possible. Matching Adjustment asset eligibility and matching criteria are also likely to be reformed in the UK to avoid the need for complex securitisations, in particular for equity release mortgages. UK insurers and the PRA may also have more room in the future for judgement around capital-setting, including more flexibility in the standard formula and a less binary model approval regime more consistent with the approach for banks, coupled with more scope for capital add-ons based on supervisory judgment.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

EU/UK regulatory divergence



The Commission is due to develop its Solvency II proposals over 2021. Many priorities in the EU's review are aligned with the UK's, most notably on the risk margin, though the EU looks more likely to retain a cost-of-capital based approach. Significant changes are also likely on long-term discount rates, affecting the euro rates in particular, as well as further changes to reduce capital requirements for insurers investing in infrastructure and long-term financing. To the extent that comparable changes are made by both the EU and UK, the level of divergence between both regimes may ultimately be reduced, although the UK is likely to move ahead of the EU with some of its higher-priority reforms, in particular the risk margin. Divergence between the UK and EU regimes in both substance and timing (including the effect of transitional adjustments where applicable) will introduce some complexity for insurers operating between the two markets. However, the UK review is also likely to make changes to facilitate cross-border business, such as potentially removing local capitalisation requirements for foreign insurers operating through UK branches. The end result will be nuanced, and internationally active insurers will need carefully to evaluate the supervisory requirements and their effects.

Investment Management

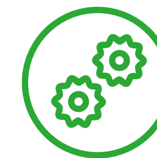
Although the UK's new IFPR will be based on the EU's IFR and IFD, the UK may take a slightly different approach in some areas. In a recent Discussion Paper,[65] the FCA suggested considering the expansion of instruments or funds that could qualify as CET1 capital for non-joint stock investment firms, and invited views on the level of detail required for calculating the Fixed Overhead Requirement. The Paper also suggested a potential 'Group Capital Test' that firms may apply as a derogation to prudential consolidation and considered exemptions from consolidated liquidity arrangements under certain circumstances. To prepare for UK implementation, firms should assess the information required to calculate the k-factors. Implementing the necessary data management processes and controls may require significant management action. Second, in terms of ICARA and risk management, firms should consider how their ICARA will be performed, meeting the holistic and outcome-focussed objectives and structure of the IFPR.

Dealing with divergence

Firms with operations in both the UK and EU should think carefully about their cross-border approach to governance, risk management and compliance. Firms face a choice between developing policies and procedures locally, or a single set across Europe (calibrated to the highest requirements), or a mix of the two. In the single set approach, a firm will have to adhere to standards more conservative than some local requirements, and should therefore assess the benefits and costs carefully, as certain regulatory requirements will lend themselves better to cross-border compliance than others. In this regard, when faced with divergence in the timing of implementation of similar requirements, a group might benefit from piloting certain risk management and/or compliance approaches in UK/European subsidiaries, before rolling out them group-wide. Adhering to higher standards may bring benefits to reputational risk management that outweigh additional compliance costs.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Operational resilience



Overview

COVID-19 has reinforced supervisors' interest in operational resilience, and we expect it to remain top of the agenda in 2021 and beyond. The near-term supervisory priority will be to ensure firms remain prepared to deal with operational disruptions from additional lockdowns, holding senior management accountable to adjust operational resilience programmes as necessary. We also expect regulators to finalise their approaches to operational resilience more broadly this year. The fact that firms generally remained operationally resilient throughout the pandemic will not in itself satisfy regulators – the regulatory agenda will ultimately require firms to test themselves against various even more challenging disruption.

In focus

- Supervisors will make more intensive use of accountability regimes to ensure firms review and update their operational resilience frameworks to incorporate lessons learnt from the pandemic.
- Supervisors will make it clear that operational resilience planning should include scenarios that are more severe than COVID-19.
- Reinforced by the COVID-19 experience, the UK's finalised regulatory approach to operational resilience will arrive in H1 2021, and will retain most of its original proposals, including the ambitious three-year implementation period.

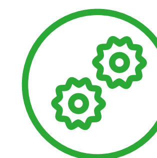
Operational resilience and COVID-19

Immediate supervisory attention in the EU and the UK is on ensuring that firms adjust their operational resilience frameworks to reflect lessons learnt from the first wave of the pandemic, and to prepare for further disruption as the situation evolves. We expect supervisors in the UK to make more intensive use of accountability regimes to track progress, holding the relevant senior manager responsible for ensuring operational resilience through extended lockdowns and in the face of threats that may yet materialise.

We expect the ECB and relevant NCAs in EU countries to take a similar approach in relation to Senior Executives responsible for overall cyber resilience strategy at FMIs.

The pandemic does not represent the most severe form of operational stress for which regulators have asked firms to prepare. Supervisors will challenge firms to consider their operational resilience against incidents that are, in the words of the BoE, 'fast, short-lived and asymmetric', and to test their readiness 'to the limit'.[66] Firms should review and update stress scenarios to ensure these reflect sufficiently severe and varied operational disruptions. This could include a scenario where the firm experiences a long-lasting data loss and is unable to provide critical services to clients for an extended period. The difficulty of predicting the kind of operational disruptions that will occur, and the sophistication of the stress testing capabilities needed to assess damage, makes this exercise challenging. Firms can use their own incident data to analyse the impact of smaller

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts



operational events and near-misses and build capabilities to understand the impact of more severe disruptions. Firms should also use 2021 to begin considering how they will deploy more sophisticated technology in the medium term to simulate major operational events.

Ongoing regulatory and supervisory work on operational resilience

Regulators continue to work on their longer-term operational resilience regulatory frameworks. The UK will finalise its approach in the first half of 2021 and, in our view, will maintain most of its original proposals in the final framework and ambitious three-year implementation period. Supervisors are already considering the resilience of firms in light of this new paradigm, using key concepts from the framework. UK-based firms should begin identifying their critical business services and mapping out key dependencies, IT assets and processes that support these. Ultimately, firms will need to demonstrate that they can maintain their critical business services within their agreed impact tolerances in a range of scenarios. For most firms, this goal will take time to achieve, putting a premium on an early start.

In the EU, the DORA will be negotiated and likely finalised by year-end. We do not expect any 2021 implementation deadlines, but firms will be able to assess the ICT risk management requirements in the proposed text against current practices, and prepare for the introduction of threat-led penetration testing (where it does not already apply) or the oversight framework for TPPs. Meanwhile, the ECB will continue to focus on firms' reliance on end-of-life systems, and controls around related IT change programmes. We also expect a greater focus on the effectiveness of IT audits, including looking for evidence that firms have followed-up on audit recommendations.

Internationally, the BCBS will look to promote cross-border regulatory convergence by finalising its Guidelines on operational resilience, which align closely to emerging supervisory expectations in several key jurisdictions. Firms should use 2021 to consider how they will comply with similar but different regimes in the EU and UK, and the extent to which work in each jurisdiction can be synergistic. Groups with a significant cross-border footprint should carry out a cost-benefit analysis to determine the balance between implementing a single operational resilience framework globally and tailoring their approach locally.

Lastly, given the significance of the Cloud in industry digitisation programmes, firms will need to keep it in mind that use of the Cloud will create operational resilience issues in need of oversight, and can therefore expect continued supervisory interest in their migration plans. The most challenging issues will be to demonstrate that they have revisited their plans in light of the pandemic and ensured that they have the necessary controls in place, while engaging early with supervisors in relation to technical risk and the governance aspects of migration. We cover the operational resilience of firms' Cloud projects in the *Deploying digitisation and innovation* chapter in more detail.

Global Foreword
Introduction
Cross-sector themes
Credit risk, financial resilience and business model viability
Final call for IBOR
Brexit – beyond the transition period
Sustainability
Conduct, culture and governance
Deploying digitisation and innovation
Financial crime in the new normal
EU/UK regulatory divergence
Operational resilience
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Sector-specific supervisory priorities

In this section, we outline a range of sector-specific supervisory priorities that are outside the scope of the preceding themes of this report.

Insurance

Investment management

Banking and capital markets

Introduction
Cross-sector themes
Sector-specific supervisory priorities
Insurance
Investment management
Banking and capital markets
Glossary
Endnotes
Contacts

Insurance

- In response to recent events, we expect sustained supervisory interest in risks such as **climate**, **cyber** and **pandemic** risks over the coming year. For these risks, **reserve adequacy and associated governance and controls**, as well as **exposure management practices**, are likely to be areas of focus. We expect ongoing discussion on whether there should be some form of **backstop** for extreme tail risk exposures. We expect both industry and government to view an industry-led solution as preferable to a public backstop. In the short term insurers will continue to manage these exposures individually, except where already covered by existing backstops.
- Following recent test cases in relation to COVID-19-related claims on business interruption insurance policies in Ireland and the UK, supervisors will pay increasing attention to **insurance policy wordings** and to what extent there is **possible ambiguity of cover** in the case of an extreme event. Supervisors may look to apply similar 'test case' approaches ex-ante for other man-made or natural catastrophe lines of business, including cyber risk. In the meantime, insurers should explore in their internal **stress testing** worst-case scenarios that assume broad interpretations of policy coverage, and identify management actions should these exceed risk appetite.
- We expect increased awareness of the importance of policy coverage, wordings and exclusions to contribute to demand for **independent third party broker expertise** when choosing insurance cover. However, supervisory scrutiny of insurance distribution chains, including in relation to **broker remuneration, pricing and product sales and oversight**, will continue to put pressure on brokers to demonstrate their value in the insurance distribution chain. Additionally, in the UK, the FCA has finalised its framework for assessing **adequate financial resources** in the firms it prudentially supervises, including insurance intermediaries.[67] This will require considerable attention and resource for brokers in 2021, and where the FCA deems firms to have potential to cause significant harm, it will conduct in-depth assessments of them as part of its evaluation of financial resource adequacy. In particular, brokers will have to assess the risks inherent in their business model, the potential harm that can be caused and explain how they could wind down the business in an orderly way.

Introduction
Cross-sector themes
Sector-specific supervisory priorities
Insurance
Investment management
Banking and capital markets
Glossary
Endnotes
Contacts

Investment management

- **Fund liquidity** will remain a key supervisory priority, in particular as a further economic downturn could crystallise concerns around the **liquidity mismatch in those funds holding illiquid assets**. Investment management firms should prioritise monitoring their funds' **liquidity, and re-visit and update their liquidity contingency plans and tools**.
- In the UK, there are a number of regulatory initiatives ongoing in response to issues concerning Woodford funds that emerged in 2019. These revealed poor governance arrangements in parts of the sector. Following some delays, we expect the BoE and the FCA to publish the findings of their review into **open-ended funds** in H1 2021 and for the FCA to conduct further work on how effectively 'host' **ACDs** undertake their responsibilities and how funds address associated conflicts of interest. New rules are likely to follow, and regulators will look to align redemption windows for funds holding less liquid assets, and establish more effective oversight of ACDs. Investment management firms should review their **redemption policies** in light of the pandemic, as well as their **governance frameworks for ACDs**.
- We expect increasing supervisory focus on **performance** and **undue costs** charged to investors by certain funds and their managers, and to what extent these funds provide **value** for consumers. In the UK, we expect the FCA over the coming months to take stock of the first round of 'Assessment of Value' reports, and this could well lead to more prescriptive guidance either to individual firms or on a thematic basis. Firms should develop clear plans to address any funds which do not fully deliver value and should satisfy themselves that their value assessments are comprehensive and will stand up to independent scrutiny.
- At the EU level, ESMA is launching a common supervisory action with a number of NCAs on the **supervision of UCITS cost and fees**. The action will look at whether firms across the EU are complying with the relevant cost provisions of the UCITS framework and the obligation not to charge investors with undue costs, reflecting the ESA's growing focus on value for money and ESMA's identification of the costs and performance of retail investment products as an EU strategic supervisory priority.

Introduction
Cross-sector themes
Sector-specific supervisory priorities
Insurance
Investment management
Banking and capital markets
Glossary
Endnotes
Contacts

Banking and capital markets

- Support measures to address and alleviate the various challenges created by COVID-19 will continue to be a focus for banking supervisors. After the initial crisis phase of the pandemic , supervisors had returned to work on other priorities, but their plans will need to be reviewed once again in light of new spikes in infection rates and the measures that some countries have taken in response.
- The BoE will complete its review of the **MREL** framework in 2021, and more generally European banks are continuing to work towards MREL targets set by resolution authorities. The latest estimate from the EBA, based on end-2018 data, quantified the shortfall in MREL for EU banks at EUR 178bn. While resolution authorities may have been prepared due to COVID-19 to consider adjusting intermediate MREL targets for banks, generally they continue to hold firm on the endpoint that banks have to reach – January 2024 for banks in the EU, and January 2022 for UK G-SIBs and D-SIBs. The exception to this, in the UK, is for mid-tier banks, which now face an extended deadline of 1 January 2023 to comply with their end-state MRELs in light of the more significant issuance challenges that they faced in 2020. Market uncertainty and an increase in the cost of debt led to reduced MREL issuance across the banking sector as a whole during the early stages of the pandemic. New issuance could continue to be difficult if there is concern about the viability of European banks (although Elke König, Chair of the SRB, told the European Parliament in October that 'the impact of Covid on ... funding plans [was] still reasonably limited'). The need to restructure or replace by the end of the CRR transition period (31 December 2021) those legacy capital instruments that are currently grandfathered but which contain ineligible structural features[68] will add further to banks' challenges. Banks will need to develop flexible issuance plans and maintain an open dialogue with supervisors and resolution authorities over the coming year.
- A number of initiatives are already in train to develop **recovery and resolution** planning for the banking sector, and several of these are due in the coming year. These represent a shift of responsibility from regulators to firms in terms of achieving resolution outcomes. For example, UK banks are due to submit their **first resolvability assessment framework** reports to the PRA by October 2021 (and make public disclosures by June 2022). The banks must also meet the BoE's requirements on resolution valuation capabilities by April 2021, and the other resolvability requirements and new policies on **OCIR** by 1 January 2022. Although the objectives of operational resilience and OCIR are distinct, there are benefits to UK banks from considering the interaction between them, and the overlap in the capabilities that underpin them, for example, concerning identification of critical/important functions, or service mapping.

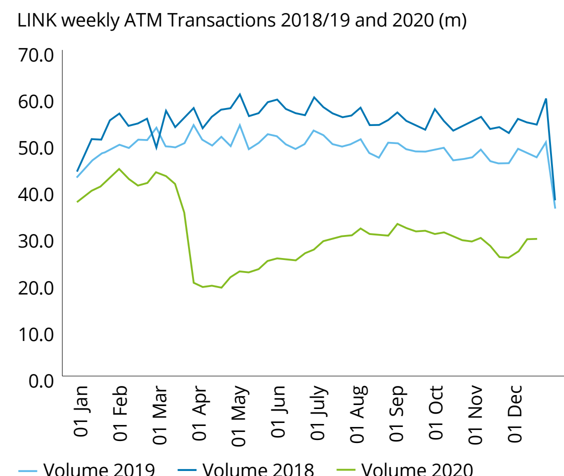
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Insurance
Investment management
Banking and capital markets
Glossary
Endnotes
Contacts

Banking and capital markets

- A statutory independent review of the operation of legislation and regulation underpinning the **UK ring-fencing regime**, is also due. And the PRA plans to introduce a new policy proposal to ensure that firms are able to **wind down their trading book** in a timely manner. Banks in the Eurozone are expected to complete **bail-in playbooks** in 2021 and to begin work on **liquidity and funding in resolution**. The SRB is also focused on ensuring that banks have in place adequate **information systems and data requirements** to provide the information necessary for resolution planning, valuation and effective resolution.
- We expect the UK's approach to implementing **FRTB requirements** to become clearer in 2021, and the BoE may move faster than the EU, given the time that the EU will need to negotiate CRR3 and the ECB will likely need thereafter to approve IMA models. UK banks should plan for UK implementation to align with the BCBS target of 1 January 2023, meaning that they may have even less time than their peers to determine which desks should apply for authorisation to use IMA and will need to use time and resources in 2021 carefully in order to ensure they are prepared.
- Although the development of scenario analysis and stress testing for climate risk are in the limelight, supervisors will continue with their **credit stress testing** exercises. An important outstanding question for the EBA's 2021 EU-wide stress test exercise is how the EBA will calibrate the scenarios, given the post-shock environment in which banks are operating. In our view, the EBA's calibration will aim to avoid the scenarios being procyclical as this could inhibit banks' ability or willingness to lend. More generally, the importance which both supervisors and banks attached to the results of stress testing during the pandemic, and the assurance and confidence that this in turn gave market participants, has reinforced the importance of stress testing as a supervisory and risk management tool. We expect this will lead to greater supervisory scrutiny through the **SREP** of banks' stress testing capabilities, especially in relation to the flexibility of their systems to run multiple scenarios, and the extent to which insights from stress testing inform business strategy and risk management decisions.
- The PRA has made clear that, now that the transition period has ended, it will move to implement a more **proportionate prudential regime for small UK banks and building societies** than is allowed under the EU framework. In 2021, we expect to see meaningful discussion as to how the PRA may tailor its approach. While there seems little appetite to compromise prudential standards, key issues such as the scope of firms eligible for the regime, and the extent to which the regime will reduce both the complexity of the prudential regime and the operational costs and challenges of compliance, will become clearer. The scope issues in particular will present challenges for the PRA, as it is increasingly clear that size alone is not a sufficient indicator of risk. Some assessment of business complexity will likely need to be incorporated into the criteria for using the simpler regime.

Introduction
Cross-sector themes
Sector-specific supervisory priorities
Insurance
Investment management
Banking and capital markets
Glossary
Endnotes
Contacts

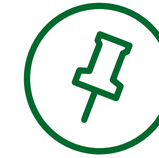
Figure 18 – UK ATM transactions much reduced year-on-year[69]



- COVID-19 has accelerated both the **closure of bank branches** with low levels of footfall and the decline in the use of cash. In the UK, the number of cash withdrawals declined markedly during the first weeks of the pandemic [Figure 18]. For regulators, this adds to concerns about the **viability of the free cash system** and the potential implications for consumers that most depend on bank branch services or cash, many of whom are potentially vulnerable customers. The European Commission has indicated that it is willing to take measures during 2021 to safeguard the acceptance and availability of cash. The UK government's Call for Evidence on this topic last year will likely lead to a decision in 2021 to give the FCA greater statutory powers to maintain access to cash. While banks may want to continue to rationalise their physical branch and ATM network as they transition to digital services and look to manage costs, they should ensure that they can clearly explain to regulators how they will protect the interests of vulnerable customers and other affected groups. Developing new hybrid service channels, such as video banking, could go some way in satisfying regulators that a shift to non-physical service delivery can be done in a way that addresses their concerns.
- We also expect significant regulatory activity in relation to the **Capital Markets Union** next year and the Commission will embark on a number of actions, most notably in relation to insolvency laws, withholding tax, supervision, investment **distribution** and **disclosure** and **shareholder engagement**. Though there will be no tangible implementation deadlines for firms in 2021, they will need to ensure they are engaging with regulators on topics that will shape the capital markets agenda for the coming years. Separately, after the adoption of the CCP Recovery and Resolution Regulation, CCP recovery and resolution is set to be a key topic, with ESMA expected to work on level two measures in 2021. EU CCPs will, in particular, need to draw up recovery plans in line with the Regulation, while banks will need to understand how their risks change given the new rules on recovery and resolution tools, and on loss allocation, which for clearing members of EU CCPs, could necessitate a review of client clearing contracts. In the UK, the resolution regime was extended to CCPs in 2014.

Introduction
Cross-sector themes
Sector-specific supervisory priorities
Insurance
Investment management
Banking and capital markets
Glossary
Endnotes
Contacts
Next

Glossary



ACD
Authorised Corporate Director

ACPR
French Prudential Supervision and Resolution Authority

AI
Artificial intelligence

AIFMD
Alternative Investment Fund Managers Directive

AMCs
Asset management companies

AML
Anti-money laundering

BaFIN
German Federal Financial Supervisory Authority

BCBS
Basel Committee on Banking Supervision

CBES
Climate Biennial Exploratory Scenario

BNPL
Buy now pay later

BoE
Bank of England

BPA
Bulk purchase annuity

CBI
Central Bank of Ireland

CCP
Central clearing counterparty

CDD
Customer due diligence

CHF
Swiss Franc

CJEU
Court of Justice of the European Union

COP26
26th UN Climate Change Conference of the Parties

CRD
Capital Requirements Directive

CRR
Capital Requirements Regulation

CSP
Cloud service provider

CTF
Counter terrorist financing

DNB
Central Bank of the Netherlands

DORA
Digital Operational Resilience Act

EBA
European Banking Authority

ECB
European Central Bank

EDPB
European Data Protection Board

EIOPA
European Insurance and Occupational Pensions Authority

EME
Emerging Market Economy

EMEA
Europe, Middle East and Africa

ESAs
European Supervisory Authorities (the EBA, ESMA and EIOPA)

ESG
Environmental, social and corporate governance

ESMA
European Securities and Markets Authority

€STR
Euro short-term rate

EU
European Union

EUR
Euro

FCA
Financial Conduct Authority

FINCEN
Financial Crimes Enforcement Network

FMI
Financial market infrastructure

FRB
Federal Reserve Board

FRTB
Fundamental Review of the Trading Book

FS
Financial services

FSB
Financial Stability Board

GDP
Gross domestic product

GDPR
General Data Protection Regulation

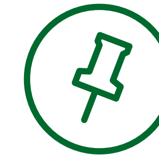
GFC
Great financial crisis

HMT
Her Majesty's Treasury

IBOR
Interbank offered rate

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Glossary



ICAAP
The Internal Capital Adequacy Assessment Process

ICARA
Internal Capital and Risk Assessment

ICAS
Individual Capital Adequacy Standards

ICE
Intercontinental Exchange

ICS
Insurance Capital Standard

ICT
Information and communications technology

IFD
Directive on the prudential supervision of investment firms

IFPR
Investment Firms Prudential Regime

IFR
Regulation on the prudential requirements for investment firms

IFRS
International Financial Reporting Standards

IMA
Internal models approach

IPU
Intermediate parent undertaking

ISDA
International Swaps and Derivatives Association

JPY
Japanese Yen

KYC
Know your customer

M&A
Mergers and acquisitions

MA
Matching Adjustment

MiFID II
Markets in Financial Instruments Directive II

ML
Machine learning

MREL
Minimum Requirement for Own Funds and Eligible Liabilities

NCA
National competent authority

NGFS
Network of Central Banks and Supervisors for Greening the Financial System

NPL
Non-performing loan

NFRD
EU Non-Financial Reporting Directive

OCIR
Operational continuity in resolution

PRA
Prudential Regulation Authority

PSD2
Payments Services Directive 2

PSR
Payment Systems Regulator

RFR
Risk-free rate

SARB
South African Reserve Bank

SCCs
Standard contractual clauses

SCR
Solvency Capital Requirement

SMCR
Senior Managers and Certification Regime

SME
Small and medium-sized enterprises

SREP
Supervisory Review and Evaluation Process

TCA
Trade and Cooperation Agreement

TCFD
Task Force on Climate-Related Financial Disclosures

TPP
Third-party provider

TPR
The Pensions Regulator

UCITS
Undertakings for Collective Investment in Transferable Securities Directive

UK
United Kingdom

USD
United States Dollar

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Endnotes

1. Speech by Antoinette M. Sayeh, IMF Deputy Managing Director, available at https://www.imf.org/en/News/Articles/2020/12/15/sp121520-sayeh-rome-investment-forum-keynote
2. Speech by Charles Randell, Chair of the FCA and PSR, available at https://www.fca.org.uk/news/speeches/financial-system-support-recovery
3. IMF, *Engines Not Yet in Sync: A Multispeed Recovery in Asia,* October 2020, available at https://blogs.imf.org/2020/10/21/engines-not-yet-in-sync-a-multispeed-recovery-in-asia/
4. Remarks by Jerome H. Powell, Chair of the Board of Governors of the Federal Reserve System, available at https://www.ecb.europa.eu/pub/conferences/html/20201111_ecb_forum_on_central_banking.en.html
5. Speech by Christine Lagarde, President of the ECB, available at https://www.ecb.europa.eu/press/key/date/2020/html/ecb.sp201111~d01e03eb9c.en.html
6. ECB, *COVID-19 Vulnerability Analysis: Results overview,* July 2020, available at https://www.bankingsupervision.europa.eu/press/pr/date/2020/html/ssm.pr200728_annex~d36d893ca2.en.pdf?dee7500437fc17e7d3f1b0d678910e40
7. BoE, *Financial Stability Report,* August 2020, available at https://www.bankofengland.co.uk/-/media/boe/files/financial-stability-report/2020/august-2020.pdf
8. FRB, *Assessment of Bank Capital During the Recent Coronavirus Event,* June 2020, available at https://www.federalreserve.gov/publications/files/2020-sensitivity-analysis-20200625.pdf
9. PRA, *Insurance Stress Test 2019 and COVID-19 stress testing: feedback for general and life insurers,* June 2020, available at https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/letter/2020/insurance-stress-test-2019-feedback.pdf
10. Remarks by Chris Woolard, then FCA Interim Chief Executive Officer, available at https://www.fca.org.uk/publication/transcripts/annual-public-meeting-2020.pdf
11. FSB, *Holistic Review of the March Market Turmoil,* November 2020, available at https://www.fsb.org/wp-content/uploads/P171120-2.pdf
12. Speech by Nick Strange, BoE Senior Technical Adviser for Operational Risk and Resilience, available at https://www.bankofengland.co.uk/speech/2020/nick-strange-oprisk-europe-resilience-in-a-time-of-uncertainty
13. US House Committee on Financial Services, available at https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=407055
14. FRB, *Interagency Examiner Guidance for Assessing Safety and Soundness Considering the Effect of the COVID-19 Pandemic on Institutions,* June 2020, available at https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20200623a1.pdf
15. Deloitte, available at https://www2.deloitte.com/us/en/insights/industry/financial-services/financial-services-industry-outlooks.html
16. FSB, *COVID-19 Pandemic: Financial Stability Impact and Policy Responses,* November 2020, available at https://www.fsb.org/wp-content/uploads/P171120-3.pdf
17. For EMEs, simple average for Brazil, Indonesia, Mexico, Russia, South Africa and Turkey. Series used for each jurisdiction (seasonally adjusted): For Brazil, loans from financial system to nonfinancial corporations and households (total credit outstanding); for European Monetary Union, money supply, loans to other Eurozone residents except government; for Indonesia, commercial and rural banks' claims on private sector (loans); for Mexico, commercial banks' credit to private sector; for Russia, bank lending, corporate and personal loans; for Turkey, bank lending to private sector; for the United Kingdom, monetary financial institutions' sterling net lending to private non-financial corporations and households; for the United States, commercial banks' loans and leases in bank credit.
18. BIS, *BIS Bulletin 21: Central banks' response to Covid-19 in advanced economies,* June 2020, available at https://www.bis.org/publ/bisbull21.pdf
19. GFC period defined as Q3 2007 to Q4 2012; COVID-19 period defined as March to December 2020. Pre-crisis GDP is Q2 2007 GDP for GFC and Q4 2019 GDP for COVID-19
20. Targeted lending operations and central bank holding of private sector assets
21. OECD (2020), IEO-data-September-2020, OECD Economic Outlook database https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&ved=2ahUKEwigkszVpofuAhWJTsAKHbIsCzkQFjAAegQIBBAC&url=http%3A%2F%2Fwww.oecd.org%2Feconomy%2Foutlook%2FIEO-data-september-2020.xlsx&usg=AOvVaw3xczt-szXiY_vddnKG_4vD (accessed on 27 November 2020)

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Endnotes

22. Refinitiv Datastream
23. IMF, *Fiscal Monitor: Policies for the Recovery,* October 2020, available at https://www.imf.org/-/media/Files/Publications/fiscal-monitor/2020/October/English/text.ashx
24. Sources: individual company accounts
25. ECB, *Financial Stability Review,* May 2020, available at https://www.ecb.europa.eu/pub/pdf/fsr/ecb.fsr202005~1b75555f66.en.pdf
26. EIOPA, Risk Dashboard, July 2020, available at https://www.eiopa.europa.eu/sites/default/files/financial_stability/risk_dashboard/eiopa-bos-20-516_july_2020_risk_dashboard.pdf
27. ECB, *Implications of Brexit for the EU financial landscape,* March 2020, available at https://www.ecb.europa.eu/pub/fie/article/html/ecb.fieart202003_01~690a86d168.en.html#toc1
28. Speech by François Villeroy de Galhau, Banque de France Governor, available at https://www.banque-france.fr/sites/default/files/medias/documents/20201007_europlace_ve_cl.pdf
29. Remarks by Valdis Dombrovskis, European Commission Executive Vice President for an Economy that Works for People, available at https://ec.europa.eu/commission/presscorner/api/files/document/print/en/ip_20_1713/IP_20_1713_EN.pdf
30. EDPB, *Recommendations 01/2020 on measures that supplement transfer tools to ensure compliance with the EU level of protection of personal data,* November 2020, available at https://edpb.europa.eu/sites/edpb/files/consultation/edpb_recommendations_202001_supplementarymeasurestransferstools_en.pdf
31. European Commission, *Draft implementing decision on standard contractual clauses for the transfer of personal data to third countries pursuant to Regulation (EU) 2016/679 of the European Parliament and of the Council,* November 2020 available at https://ec.europa.eu/info/law/better-regulation/
32. European Commission, *Public consultation on the review of the Alternative Investment Fund Managers Directive,* October 2020, available at https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/2020-aifmd-review-consultation-document_en.pdf
33. The Investment Association, *Investment Management in the UK 2019-2020: The Investment Association Annual Survey,* September 2020, available at https://www.theia.org/sites/default/files/2020-09/20200924-imsfullreport.pdf
34. FCA, *Discussion Paper 18/8: Climate Change and Green Finance,* October 2018, available at https://www.fca.org.uk/publication/discussion/dp18-08.pdf
35. ECB, *Guide on climate-related and environmental risks: Supervisory expectations relating to risk management and disclosure,* November 2020, available at https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202011finalguideonclimate-relatedandenvironmentalrisks~58213f6564.en.pdf
36. PRA, *Managing climate-related financial risk – thematic feedback from the PRA's review of firms' Supervisory Statement 3/19 (SS3/19) plans and clarification of expectations, July 2020,* available at https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/letter/2020/managing-the-financial-risks-from-climate-change.pdf?la=en&hash=A6B4DD1BE45B2762900F54B2F5BF2F99FA448424
37. ACPR, *Scenarios and main assumptions of the ACPR pilot climate exercise,* July 2020, available at https://acpr.banque-france.fr/sites/default/files/medias/documents/20200717_main_assumptions_and_scenarios_of_the_acpr_climate_pilot_exercise.pdf
38. ECB, *Guide on climate-related and environmental risks: Supervisory expectations relating to risk management and disclosure,* November 2020, available at https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202011finalguideonclimate-relatedandenvironmentalrisks~58213f6564.en.pdf
39. FCA, *Discussion Paper 18/8: Climate Change and Green Finance,* October 2018, available at https://www.fca.org.uk/publication/discussion/dp18-08.pdf
40. Speech by Andrea Enria, ECB Chair, available at https://www.bankingsupervision.europa.eu/press/interviews/date/2020/html/ssm.in20200925~0a49bf3ea9.en.html
41. FCA, *FCA highlights continued support for consumers struggling with payments,* October 2020, available at https://www.fca.org.uk/news/press-releases/fca-highlights-continued-support-consumers-struggling-payments

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Endnotes

42. EBA, *EBA report on the benchmarking of diversity practices at European Union level under Article 91(11) of Directive 2013/36/EU, February 2020,* available at https://eba.europa.eu/eba-calls-measures-ensure-more-balanced-composition-management-bodies-institutions
43. Opinion piece by Yves Mersch, Member of the Executive Board of the ECB, available at https://www.bankingsupervision.europa.eu/press/interviews/date/2020/html/ssm.in201001~1f7f9235a4.en.html
44. Speech by Burkhard Balz, Member of the Executive Board of the Deutsche Bundesbank, available at https://www.bundesbank.de/en/press/speeches/covid-19-and-cashless-payments-has-coronavirus-changed-europeans-love-of-cash--848678#nb1
45. Speech by Tom Mutton, BoE FinTech Director, available at https://www.bankofengland.co.uk/-/media/boe/files/speech/2020/response-and-recovery-fintech-during-the-covid-crisis-and-beyond-speech-by-tom-mutton.pdf?la=en&hash=98978EBC816E746878F28DCA4F4D2ED929E66A0C
46. BoE, *Quarterly Bulletin 2020 Q4: The impact of Covid on machine learning and data science in UK banking,* December 2020, available at https://www.bankofengland.co.uk/quarterly-bulletin/2020/2020-q4/the-impact-of-covid-on-machine-learning-and-data-science-in-uk-banking
47. BoE, *Quarterly Bulletin 2020 Q4: The impact of Covid on machine learning and data science in UK banking,* December 2020, available at https://www.bankofengland.co.uk/quarterly-bulletin/2020/2020-q4/the-impact-of-covid-on-machine-learning-and-data-science-in-uk-banking
48. European Commission, *Retail Payments Strategy for the EU,* September 2020, available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020DC0592&from=EN
49. HMT, *Payments Landscape Review: Call for Evidence,* July 2020, available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/904140/2020_template_PLR_CfE_27072020_final.pdf
50. FSB, *Enhancing Cross-border Payments: Stage 3 roadmap,* October 2020, available at https://www.fsb.org/wp-content/uploads/P131020-1.pdf
51. Speech by Tom Mutton, BoE FinTech Director, available at https://www.bankofengland.co.uk/-/media/boe/files/speech/2020/response-and-recovery-fintech-during-the-covid-crisis-and-beyond-speech-by-tom-mutton.pdf?la=en&hash=98978EBC816E746878F28DCA4F4D2ED929E66A0C
52. FCA, *Coronavirus and safeguarding customers' funds: additional guidance for payment and e-money firms, July 2020,* available at https://www.fca.org.uk/publication/finalised-guidance/coronavirus-safeguarding-customers-funds-additional-guidance-payment-e-money-firms.pdf
53. FSB, *The Use of Supervisory and Regulatory Technology by Authorities and Regulated Institutions: Market developments and financial stability implications, October 2020,* available at https://www.fsb.org/wp-content/uploads/P091020.pdf
54. World Bank and CCAF (2020) The Global Covid-19 FinTech Regulatory Rapid Assessment Report, World Bank Group and the University of Cambridge
55. Speech by Valdis Dombrovskis, European Commission Executive Vice President for an Economy that Works for People, available at https://ec.europa.eu/commission/presscorner/detail/en/speech_20_2031
56. ESAs, *The AML/CFT Colleges Guidelines,* December 2019, available at https://esas-joint-committee.europa.eu/Publications/Guidelines/joint-guidelines-on-cooperation-and-information-exchange-on-AML-CFT.pdf
57. UK Finance, *2020 Half year fraud update,* September 2020, available at https://www.ukfinance.org.uk/system/files/Half-year-fraud-update-2020-FINAL.pdf
58. Speech by Julia Hoggett, FCA Director of Market Oversight, available at https://www.fca.org.uk/news/speeches/market-abuse-coronavirus
59. Letter from Catherine Lewis La Torre, British Business Bank Chief Executive, available at https://committees.parliament.uk/publications/3313/documents/31202/default/
60. Speech by Julia Hoggett, FCA Director of Market Oversight, available at https://www.fca.org.uk/news/speeches/market-abuse-coronavirus

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Endnotes

61. BaFIN, available at https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Meldung/2020_Corona/meldung_2020_04_03_corona_virus8_MAR_en.html
62. Speech by Julia Hoggett, FCA Director of Market Oversight, available at https://www.fca.org.uk/news/speeches/market-abuse-coronavirus
63. HMT, *Policy statement: Prudential standards in the Financial Services Bill,* June 2020, available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/893792/Prudential_policy_draft_policy_statement_V4.pdf
64. Statement by Rishi Sunak MP, Chancellor of the Exchequer, available at https://questions-statements.parliament.uk/written-statements/detail/2020-06-23/HCWS309
65. FCA, *Discussion Paper 20/2: A new UK prudential regime for MiFID investment firms,* June 2020, available at https://www.fca.org.uk/publication/discussion/dp20-2.pdf
66. Speech by Nick Strange, BoE Senior Technical Adviser for Operational Risk and Resilience, available at https://www.bankofengland.co.uk/speech/2020/nick-strange-oprisk-europe-resilience-in-a-time-of-uncertainty
67. FCA, *Finalised Guidance 20/1: Our framework: assessing adequate financial resources,* June 2020, available at https://www.fca.org.uk/publication/finalised-guidance/fg20-1.pdf
68. Ineligible features include, but are not limited to: dividend pushers (if one instrument is paid a dividend, then the instrument in question must also be paid); dividend blockers (if this instrument is not paid a dividend, other instruments may not be paid) and other features that interfere with optionality of dividend payments or deliberately obfuscate the relative subordination of capital instruments.
69. LINK, available at https://www.link.co.uk/about/statistics-and-trends/

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

Contacts

David Strachan
Partner, Head of Centre for Regulatory Strategy, EMEA
dastrachan@deloitte.co.uk
+44 20 7303 4791

Andrew Bulley
Partner, Centre for Regulatory Strategy, EMEA
abulley@deloitte.co.uk
+44 20 7303 8760

Thomas Spellman
Partner, FS Risk Advisory Leader
thspellman@deloitte.co.uk
+44 20 7303 0019

Cindy Chan
Partner, FS Industry Leader, Risk Advisory
cichan@deloitte.co.uk
+44 20 7303 5836

Global Foreword
Introduction
Cross-sector themes
Sector-specific supervisory priorities
Glossary
Endnotes
Contacts

CENTRE *for*
REGULATORY STRATEGY
EMEA

The Deloitte Centre for Regulatory Strategy is a powerful resource of information and insight, designed to assist financial institutions manage the complexity and convergence of rapidly increasing new regulation.

With regional hubs in the Americas, Asia Pacific and EMEA, the Centre combines the strength of Deloitte's regional and international network of experienced risk, regulatory, and industry professionals – including a deep roster of former regulators, industry specialists, and business advisers – with a rich understanding of the impact of regulations on business models and strategy.

Download this report, and more like it, at Deloitte.co.uk/ECRS

Deloitte.

This publication has been written in general terms and we recommend that you obtain professional advice before acting or refraining from action on any of the contents of this publication. Deloitte LLP accepts no liability for any loss occasioned to any person acting or refraining from action as a result of any material in this publication.

Deloitte LLP is a limited liability partnership registered in England and Wales with registered number OC303675 and its registered office at 1 New Street Square, London EC4A 3HQ, United Kingdom.

Deloitte LLP is the United Kingdom affiliate of Deloitte NWE LLP, a member firm of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"). DTTL and each of its member firms are legally separate and independent entities. DTTL and Deloitte NWE LLP do not provide services to clients. Please see www.deloitte.com/about to learn more about our global network of member firms.

© 2021 Deloitte LLP. All rights reserved.

Designed and produced by Deloitte CoRe Creative Services, London. 585667