European Securities and Markets Authority

28 May 2021
ESMA50-164-4575

OPINION

Collection of information for the effective monitoring of systemic risk under Article 24(5), first subparagraph, of the AIFMD

1 Legal basis

1. ESMA's competence to deliver an opinion is based on Article 29(1)(a) of Regulation (EC) No 1095/2010 (the 'Regulation'). In accordance with Article 44(1) of the Regulation the Board of Supervisors has adopted this opinion.

2 Background

2. ESMA has published a final report on guidelines on reporting obligations under Articles 3(3)(d) and 24(1), (2) and (4) of the Alternative Investment Fund Managers Directive[1] (AIFMD). These guidelines (see Annex II of ESMA/2013/1339[2]) aim at clarifying the content of the information that alternative investment fund managers (AIFMs) should provide to their national competent authorities (NCAs) when complying with the provisions of Articles 3(3)(d) and 24(1), (2) and (4) of the AIFMD.

3. The reporting template set out in Annex IV of Regulation 231/2013 implementing the AIFMD (the Regulation) provides for an extensive set of information to be reported by AIFMs to their NCAs. However, ESMA believes that the effective monitoring of systemic risk potentially caused by one AIFM or a group of AIFMs would be facilitated by NCAs' also adopting a common approach when making use of their power to require additional information under Article 24(5), first sub-paragraph, of the AIFMD. This additional information would also allow for a more comprehensive oversight of the activities of AIFMs by supplementing the reporting in such areas as risk measures and short positions.

4. In this opinion, ESMA provides details on a set of additional information that, in its view, NCAs could require AIFMs to report on a periodic basis pursuant to Article 24(5), first sub-paragraph of the Directive

3 Information relevant for effective monitoring of systemic risk

- Information on the number of transactions

[1] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010

[2] 2013/ESMA/1339

5. ESMA believes that information on the total number of transactions carried out using a high frequency algorithmic trading technique, as defined in the forthcoming revised Markets in Financial Instruments Directive (MiFID II), together with the corresponding market value of buys and sells in the base currency of the AIF over the reporting period, could be usefully collected by NCAs. ESMA is of the view that it would be appropriate for NCAs to require this information to be reported following the entry into force of MiFID II.

- Information on geographical focus based on the domicile of investments made

6. ESMA would see merit in NCAs' requiring that information on the geographical focus also be expressed as a percentage of the total value of assets under management calculated in accordance with Articles 2 and 10 of the Regulation, so that the impact of financial derivative instruments is better taken into account.

- Information on short positions

7. According to the reporting template set out in the Regulation, AIFMs shall specify the five most important instruments in which the AIF is trading and whether the positions are short or long. When AIFMs report short positions, ESMA considers it desirable for NCAs to require that this information be supplemented by an indication of whether the position is used to hedge a position with a similar economic exposure. In that context, ESMA believes it would be appropriate for NCAs to require information on the extent of the hedging expressed as a percentage.

- Information on risk measures

8. Where relevant, according to the predominant AIF type of the AIF, ESMA would see merit in NCAs' requiring information on the Value at Risk (VaR) of the AIFs to be reported. For example, such information would be particularly relevant for AIFs pursuing hedge fund strategies.

9. ESMA would consider it appropriate for NCAs to require the VaR of the AIF to be calculated using one of the following three methodologies: Monte Carlo simulation, Historical simulation or Parametric VaR (ESMA/2013/1340 Opinion). The analysis should be carried out in accordance with the following parameters: (a) one-tailed confidence interval of 99%; (b) holding period equivalent to 1 month (20 business days); (c) effective observation period (history) of risk factors of at least 1 year (250 business days) and be expressed as the effect on the portfolio (all positions including derivatives) as a percentage of the total net asset value of the fund at the end of the reporting period. With regard to the rescaling of the VaR from a different confidence interval and different holding period, this should be done in line with the principles laid down in section 3.6.1 of the CESR's Guidelines CESR/10-788.

9a. The VaR fields of the report are optional, but as already indicated in this opinion, ESMA sees a merit in NCAs requiring the information from all AIFs where it is relevant. VaR might not be relevant for Private Equity funds and Real Estate funds. If the metric is not considered relevant by managers of other types of funds, an explanation should be given in the "Risk measure description" field (data field 147).

9b. The following examples could be considered:

- If an AIF with a NAV of 50M EUR has an estimated probability of 1% to see a portfolio decline of more than 5M EUR in the next 20 business days (1 month) then it should report "10" (for a VaR of 10%).
- In case an AIF has no Value-at-Risk to report, then the figure to be reported under "Value-at-Risk" would be "0". In that case, "No Value-at-Risk can be reported" would be reported in the Risk Measure Description field (147) and an explanation should also be provided.

10. Moreover, ESMA believes that, where relevant according to the investment strategy of the AIF, further information such as the portfolio's sensitivity to a change in FX rates or commodity prices would constitute useful information to be required by NCAs.

10a. ESMA would consider that the Net FX delta shall be used to analyse portfolio's sensitivity to movements in FX prices. The following case could be considered: assume all currencies the AIF is exposed to depreciate by 1% relative to the fund's base currency at the end of the reporting period. In this case, the AIFM shall report the effect on the total net asset value of the AIF (taking into account all the positions (including derivative positions) of the portfolio) as a monetary value in base currency. In the case of derivative positions, a depreciation of 1% in the value of the underlying should be considered, and not in the value of the derivative. It shall report: (i) a negative value if the variation of the net asset value is negative;(ii) a positive value if the variation is positive and (iii) a zero if the AIF is neutral or not exposed at all to this risk. In case a measure of risk is not applicable for an AIF or when AIFM report a zero value, the reasons should be explained in the "Risk Measure Description" (data field 147).

10b. More precisely, the following examples could be considered:

- Assume the AIF has a well-diversified geographical/currency exposure and the euro as base currency. If, at the quarter-end, the NAV sensitivity of this AIF to a 1% depreciation against euro of all currencies is -0.5% and if its NAV is 100M EUR, then the figure to be reported under the field "Net FX delta" is "-500000" (EUR).
- Assume an AIF has no exposure to FX risk, then the figure to be reported under "Net FX delta" would be "0". In that case, "No exposure to FX risk" would be reported in the Risk Measure Description field (147)."

10c. ESMA would consider that the Net commodity delta shall be used to analyse portfolio's sensitivity to movements in commodity prices. The following case could be considered: assume the prices of all physical commodities the AIF is exposed to directly or through synthetic exposure (gold included, derivatives and delta-one products included), as expressed in base currency, decrease by 1% at the end of the reporting period. In the case of derivative positions, a decline of 1% in the value of the underlying should be considered, and not in the value of the derivative. In this case, the AIFM shall report the effect on the total net asset value of the AIF (taking into account all the positions (including derivative positions) of the portfolio) as a monetary value in base currency. It shall report: (i) a negative value if the variation of the net asset value is negative; (ii) a positive value if the variation is positive and (iii) a zero if the AIF is neutral or not exposed at all to this risk. In case a measure of risk is not applicable for an AIF or when AIFM report a zero value, the reasons should be explained in the "Risk Measure Description" (data field 147).

10d. More precisely, the reporting expectations are shown in the examples below:

- Assume an AIF has investment in commodity derivatives and that, at the quarter-end, the NAV sensitivity of this AIF to a 1% decline in all commodity prices is -0.5% and that its NAV is 100M EUR, then the figure to be reported under the field “Net commodity delta” would be “-500000” (EUR).
- Assume an AIF has no commodity exposure, then the figure to be reported under “Net commodity delta” would be “0”. In that case, “No exposure to commodity risk” would be reported in the Risk Measure Description field (147).

- Information on non-EU master AIFs not marketed in the Union

11. Reporting obligations under Article 24(2) of the AIFMD cover only EU AIFs or AIFs marketed in the Union. This means that AIFMs are not required to report information under Article 24(2) of the AIFMD for non-EU AIFs that are not marketed in the Union.

12. Therefore, in order to have a comprehensive set of information for a proper assessment of systemic risk, ESMA considers it desirable for NCAs to require AIFMs that manage non-EU master AIFs that are not marketed in the Union to report, in addition to the information under Article 24(1), for these AIFs the information requested by Article 24(2) of the AIFMD in so far as one of the feeder AIFs of these master AIFs is an EU AIF or is marketed in the Union. However, ESMA does not consider it useful for NCAs to require this information to be provided if the non-EU master AIFs and the feeder AIFs mentioned above do not have the same AIFM.