afme/
Finance for Europe

Impact of PRIIPs on Retail Activity in Corporate Bonds

afme/
Finance for Europe

Contents

1. Impact of the PRIIPs rules as they stand: the post 1 January 2018 market for vanilla corporate bonds
   - Existing corporate bonds/access by retail investors
   - New issues
2. Considerations that discourage corporate issuers from preparing KIDs (see attachment)

afme/ Finance for Europe

Retail investors unable to access sections of the bond market - key issues since January 2018

- No grandfathering - which instruments are PRIIPs?
  - an AFME member has estimated (based on a review of Bloomberg information in late February) that there are at least 600,000 existing vanilla corporate bonds which may be PRIIPs
  - Uncertainty as a result of differing approaches by EU regulators - e.g. rights issues
- Significant impact of scope uncertainty
  - Primary markets:
    - use of the ICMA 1 (professionals only) approach in at least 80 issuances of vanilla corporate bonds. AFME members report no sales to retail of bonds in this situation by private banks/distributors
    - in markets where Make Whole clauses (MWC) and other common clauses generate uncertainty as to whether vanilla bonds may be PRIIPs, the absence of KIDs means no sales to retail
    - in some local markets where large corporate issuers do not use MWCs and change of control clauses, sales to High Net Worth retail continue
  - Secondary markets:
    - some AFME members report a reduction of the order of 20-25% of retail corporate bond flow - in specific markets this can be much greater (e.g. a member reports 76% decrease in retail bond sales in January 2017 vs January 2018)
    - AFME members predict that impact will increase over the next 2/3 years as more and more existing issues mature and cannot be replaced in retail client portfolios due to new issues being either closed to retail (ICMA 1 approach) or not having KIDs.
    - some AFME members consider this will mean that retail investors will have to look for alternative investment opportunities, which could include:
      - Collective investment schemes investing in bonds (increased costs)
      - Structured products (increased costs and opacity)
      - Loan participation notes (increased risk)

afme/
Finance for Europe

Practical challenges in preparing KIDs for corporate bonds

- Who is the manufacturer?
  - are non-financial corporate issuers in scope of the 'manufacturer' definition?
  - Who has the power to enforce the rules against corporate issuers (who are usually not regulated)?
- Drawing up a KID creates liabilities for the issuer
  - vs EEA investors (e.g. if KID inconsistent with other documents relating to the issue)
  - vs EEA regulators (if KID inconsistent with KID regulation requirements)
  - vs non-EEA investors (who do not receive the KID and could argue that the offer documents aimed at them, without a summary risk indicator and PRIIPS performance scenarios, therefore omit material information)
- Ongoing review obligations
  - How to comply given updating requirements imposed by other legal requirements

AFME members report that issuers have (since 1st January) avoided producing a KID by: (a) not selling to retail (the majority); or (b) dropping Make Whole and other common clauses (the minority)