AUSTRIAN FMA · FINANCIAL MARKET AUTHORITY

FACTS AND FIGURES TRENDS 2024 AND STRATEGIES

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MEDIUM-TERM RISK ANALYSIS 2024-2028

“CRISIS IS THE NEW NORMAL FOR THE FINANCIAL SYSTEM …”

The risk map has been completely transformed over the past few years. The financial markets have been hit by one exogenous shock after the other. No sooner had hopes turned to stability, security and growth than another unexpected external factor would plunge the markets into turmoil, causing stress for many market participants, generating uncertainty and once again massively clouding the outlook for the future. These have ranged from the COVID-19 pandemic and Russia’s war of aggression against Ukraine to commodity, energy and material bottlenecks that have paralysed the real economy and geopolitical realignment, in turn forcing a restructuring of global economic relations. The current shock is the campaign of terror being conducted by Hamas against Israel, which is dangerously fuelling political tensions and armed conflict in a region that is particularly sensitive for the global economy. These exogenous shocks are factors that financial market supervisors and stability watchdogs did not have on their radar, and actually could not have predicted at all.

Despite all these challenges, the financial markets have ultimately proven to be resilient and stable in the face of all the volatility, and the financial sector has proven to be robust in the face of crisis. A few key figures as at the middle of 2023:

- **Austria's banks** have never had higher levels of Common Equity Tier 1 capital, which now stands at around 16.5%. This is also roughly in line with the average for the eurozone as a whole. Profitability is at record levels; at 1.1% their capital return is significantly higher than the euro area average of 0.7%.
- **Insurance undertakings** have very high levels of solvency. On average, they fulfil their solvency capital requirement (SCR) by more than 250%. Their level of own funds to absorb unforeseen losses is therefore more than twice as high as required.
- **Asset managers** such as *Pensionskassen*, corporate provision funds and investment funds were able to stabilise the massive slump in share prices triggered by the exogenous shocks and resulting capital market turbulence, and are slowly recovering their losses.

Crucially important in this regard was the fact that politicians, regulators and supervisors learned the right lessons from the global financial crisis of 2008, particularly in Europe. Cross-border regulatory guidelines were put in place for the borderless single market for financial services, existing regulations were evaluated, revised and harmonised in light of the experience gained from the crisis, and any regulatory loopholes were remedied. Supervision has been Europeanised. Strong European institutions have been created based on the network of national supervisors, thus maintaining market proximity while also guaranteeing standardised and effective application and enforcement of the law on a Europe-wide basis. Today, regulation and supervision is carried out throughout Europe in accordance with best practice in the individual Member States. Regulatory and supervisory arbitrage between individual states has largely been stopped.

The euro countries have built a banking union alongside the single currency, on a foundation of common harmonised rules supported by three pillars: joint supervision, joint resolution and joint deposit protection. Supervision and resolution have been operating for years under the strong lead of the European Central Bank (ECB) and the European Single Resolution Board (SRB), but in conjunction with and supported by the network of national supervisory partners. Although deposit protection has not yet been Europeanised, it has at least been possible to achieve a minimum level of harmonisation across Europe. The financial crisis intervention pots, be it the deposit guarantee scheme, the resolution fund or ultimately the European Stability Mechanism (ESM), are already well funded and are constantly being strengthened, thus building confidence in Europe's financial stability and problem-solving capacity.

All of these measures have proven their worth in overcoming the huge challenges of recent years.

However, this cannot be a reason to sit back and relax. The series of exogenous shocks has shown that supervisors and financial market participants must be constantly prepared to manage crises, regardless of their source. Risk and crisis management must be flexible enough that it can even be applied to shocks and challenges that nobody dared imagine.

FINANCIAL AND NON-FINANCIAL RISKS ARE INCREASING

Recent developments show that both the financial and non-financial risks facing the European and Austrian financial sector have increased. In addition to the exogenous shocks, in a clear reflection of geopolitical tensions, there has also been a significant economic slowdown. Economic researchers are still hoping that the recession will be mild, but it is still expected to last for some time. Above all, the huge jump in inflation from the 2021 year-end onwards is proving difficult to get under control, not least in Austria. The resulting forced normalisation of monetary policy brought the phase of low interest rates spanning more than ten years to an abrupt halt. Central banks around the world have been significantly raising their key interest rates since summer 2022 in the fight against inflation. After many years keeping rates hovering around zero, the ECB has implemented ten interest rate hikes, with key rates at 4.5%, 4.75% and 4.0% respectively. This is their highest level since the launch of the monetary union in 1999.

The weak economic outlook, soaring inflation and the rise in interest rates are impacting the ability of households, businesses and governments to service their debts. The tighter financing conditions are severely restricting their economic room for manoeuvre.

And the economic sword of Damocles continues to loom large: geopolitical tensions and disputes could trigger energy or raw material shortages and hold up or even

"Austria's financial market and all of its market participants are facing huge challenges. The abrupt turnaround in interest rates, the significant inflation risk and a weak global economic outlook all put massive pressure on businesses and households and their ability to pay their bills and service their debts."

FMA Executive Directors Eduard Müller and Helmut Ettl

break global supply chains. The geopolitical and global economic situation remains extremely tense, uncertain and fragile.

This toxic mix prompted the European Systemic Risk Board (ESRB) to issue a general risk warning in 2022, for the first time in its thirteen years of existence:

- **Firstly,** given the gloomy growth prospects, significantly increased inflation and tighter financing conditions, companies and households' finances are being placed under huge stress. This is also putting a massive strain on their ability to service their debt.
- **Secondly,** there is a high risk of dramatic falls in prices and the value of certain assets, in turn creating serious risks for financial stability. This could also trigger significant impairment requirements in the non-banking sector and for shadow banks, which in turn harbours the risk of distress sales that could further accelerate the decline in value, increase market volatility and create liquidity bottlenecks.
- **Thirdly,** the deterioration in the macroeconomic outlook combined with heightened geopolitical tensions is increasing banks' credit, market and financing risk, which is why forward-looking and prudent management of these risks is vital. Structural factors are also having a negative impact on the resilience of financial service providers. These factors include overcapacity in the market, competition from new providers of financial services, and both cyber and climate risk.
- **Fourthly,** the systemic risk of cyber incidents is steadily climbing in light of the intensifying geopolitical tensions.

According to the ESRB, there is also a particular danger that these risks could materialise at the same time and mutually aggravate each other.

Fortunately, there has not yet been any occurrence of the worst case scenario. However, the risks have not been banished. Some risks, in fact, have already materialised:

- Households' ability to manage their debts has deteriorated markedly. Although the labour market situation remains good and stable, real disposable incomes are coming under massive pressure due to high inflation and the spiralling cost of living. At the same time, savings and investments are increasingly losing value and purchasing power due to real rates of return falling well below zero. Another factor is the financial burden of borrowing, which is growing quickly and significantly, especially in the case of variable-rate loans.

- Certain assets have already seen their value slashed. The rise in interest rates has, for example, significantly depressed the prices of low-interest, government and mortgage bonds, particularly long-term paper, one of the most important asset classes in asset management portfolios. This has already sparked high volatility in some markets, such as the UK gilt market, despite UK bonds being considered a particularly secure investment.
- The sudden, sharp rise in interest rates has halted what has been a long-lasting property boom in almost all of the eurozone countries. Construction volumes have fallen significantly across Europe, the financing of mortgage loans and commercial property has collapsed, and the real estate and construction industry has generally come under severe pressure. In Austria, property prices are stagnating. They failed to keep up with the huge rise in inflation in 2022/23 and are now actually falling slightly for the first time. It has become more difficult to buy a home given the huge rise in mortgage interest rates coupled with increased pressure on disposable household income. Meanwhile, the commercial property market has also come under severe pressure. The trend towards working from home, particularly since the pandemic, has quietened demand for office premises. Excessive real estate valuations have already had to be reduced and the prices of property shares and property funds are coming under strong pressure. This economic sector is suffering particularly badly from weak economic growth, rising inflation and climbing interest rates. Higher vacancy rates are reducing income, which is depressing the value of real estate. Such a situation then makes refinancing more difficult and increases the pressure to sell off properties in order to fulfil financial obligations. This in turn increases the stress on the market and exacerbates the structural challenges (namely sustainability and digital transformation) pro-cyclically. Due to the high level of debt financing in the real estate sector, any problems on this market also pose the risk that they will ultimately spill over onto the financial markets.

As challenging as the rise in interest rates is right now for households and companies, which have enjoyed historically favourable rates for many years, it is a long-awaited godsend for financial service providers such as banks and insurance undertakings that operate in interest-sensitive business. This is because a higher interest rate level creates scope for a wider interest margin and with it higher interest income. The banks could also afford to pass on the rise in debit interest rates more quickly and significantly than credit rates. This has led to record profits despite the difficult times, also due to the cost management forced by the low interest rate phase. Banks are currently earning as well as they have done for years.

That being said, the fragile geopolitical situation and the gloomy economic outlook also present them with major challenges.

- The currently shrinking economy and rather weak growth, at least in the medium term, combined with higher interest rates, are eroding the quality of the assets on their books. This requires significant value adjustments and provisioning. At the same time, the weak state of the economy and high interest rates are curbing financing and therefore business activity, which is eating into profitability.

- Ultimately, higher interest rates also mean higher refinancing costs for banks. This puts the interest margin under pressure again, and the longer it lasts, the greater the pressure.
- The portfolio of old fixed-interest receivables (particularly bonds with long maturities) loses value as interest rates rise, creating huge losses as soon as this fall in value has to be realised.

The banking crises that flared up in the USA and Switzerland at the beginning of the year must be viewed as a warning. It was only thanks to swift and decisive intervention on the part of politicians, central banks and regulators that these situations could be contained and contagion effects avoided. However, the causes of the flashpoints were very different.

In Switzerland, Credit Suisse failed because it was unable to get a grip on its corporate culture for many years. A series of corruption and money laundering scandals took their toll, encompassing fraud, business relationships with dubious business partners such as the hedge fund Archegos or the Greensill Fund and even spying on the bank's own managers, all of which fundamentally undermined confidence in the bank's management and governance over the years. When even a major shareholder publicly refused to provide any more money, confidence in the bank finally imploded and it faced the very real possibility of collapse. The government, supervisory authority and central bank all had to step in and force a takeover by Switzerland's second major bank, UBS, in order to preserve financial market stability and avert a domino effect similar to the collapse of US investment bank Lehman Bros in 2008.

"Financial service providers should engage in proactive risk management and further strengthen their capital base and risk-bearing capacity by pursuing a prudent dividend distribution policy. They should also continue to improve their cost management through consistent use of the new digital opportunities."

The fall of Credit Suisse dramatically demonstrated the enormous impact that negligence in the management of operational risks can have, whether deliberately or through lack of due care and attention. Corruption, money laundering, violations of sanctions and excessive greed can now damage a bank's reputation beyond repair, and the loss of trust can deprive the bank of its business foundation.

The Credit Suisse case shows how important it is to always focus on operating cleanly in a financial centre. And it also shows that it is possible to take even a globally significant bank out of the market in an orderly fashion by working together.

The crisis facing some regional banks in the USA also had regulatory causes. In order to promote the regional economy, Donald Trump, who was US president at the time, unceremoniously raised the balance sheet threshold above which the strict global Basel III capital and supervisory standards also applied to a bank in the USA. As a result, these regional banks ceased to be bound by these standards and came under the supervision of the regional authority. The best-known of these regional banks was Silicon Valley Bank (SVB) with consolidated total assets of just over $200 billion and which specialised in financing high-tech companies and start-ups. However, these companies also held their cash positions and surplus liquidity at this bank, which invested their money in long-term government and mortgage bonds.

When interest rates started to soar, the tech boom shuddered to a halt and the bank's customers needed their money back. At the same time, rising interest rates caused the prices of the low-interest long-term bonds to fall. The bank had no option but to realise huge price losses. However, its refinancing subsequently failed because its customer base comprised a small, closed community that immediately shared updates on its social networks as soon as any one customer got wind of a problem. This triggered a digital bank run in a matter of seconds. The Federal Deposit Insurance Corporation (FDIC) had to remove the bank from the market in an orderly fashion, making the SVB case the second largest orderly bank closure in US history after Washington Mutual in 2008. The crisis at the US regional banks did however keep the global financial world on tenterhooks for some time. Fears of bankruptcies and increased funding requirements for other banks triggered significant price losses for bank shares across the world.

There are two main lessons to be learned from the Silicon Valley Bank case:

- Regulation and supervision must not be misused for structural policy or business promotion purposes. The strict Basel III global supervisory regime must be applied consistently to all banks. It already offers sufficient room for manoeuvre so that the strict rules can be applied proportionately taking into account the complexity and riskiness of the business model. As a regulator and supervisor in Austria, a market with a high proportion of medium-sized and small banks, the FMA faces a particular challenge here, not least because the Austrian banking structure reflects the small and medium-sized structure of the real economy, thus ensuring market proximity and specific expertise.
- Furthermore, the crisis at the US regional banks dramatically demonstrated how digital change, with the impact of social media and digital finance, is also challenging crisis management. In the digital financial world, huge amounts of funds can be withdrawn in a matter of seconds, and customers can communicate with each other in real time and coordinate their actions effortlessly.

The series of exogenous shocks that have presented such a challenge to the stability and crisis resilience of the financial markets and their participants in recent years has also overshadowed or at least temporarily obscured structural developments that are fundamentally changing our society and economy now: digitalisation, the fight against climate change, far-reaching changes in consumer behaviour and a new omnipresent ethical imperative.

THE DIGITAL TRANSFORMATION

Digitalisation is advancing apace and is profoundly changing our economy and our society. Nearly all of us have a smartphone nowadays, and nearly everyone surfs the internet, uses social media and takes advantage of digital tools for life admin and leisure activities. And when it comes to the world of money and finance, nearly everything can be done digitally in real time too: paying, saving, investing, financing, planning for the future or insuring – whenever and wherever we want.

The digital transformation has also fundamentally changed the financial sector and financial markets. Established providers have long since expanded their analogue business models based on a local presence and personal advice to include a digital

“The digital transformation creates opportunities and risks. We therefore focus on ICT and cybersecurity alongside the incorporation of crypto assets into our regulatory and supervisory system.”

offering, if not largely replaced their traditional model. Innovative providers have established new technological business models, taken traditional financial products a step further and also created entirely new products. Creative technologies such as cloud computing, machine learning, artificial intelligence, large language models, data mining, data engineering and big data are constantly driving change.

However, there is more to technological progress and innovation than new opportunities. There are also risks. This poses major challenges for regulation and supervision.

The FMA is therefore monitoring developments on the Austrian financial market very closely. The aim is to identify and analyse new trends and drivers of development and to identify and address risks and contagion channels.

For example, the number of cyber attacks and cases of data theft has been rising sharply worldwide and in Austria for years. The attack scenarios are becoming more and more technically sophisticated. Espionage, sabotage and blackmail have also long been part of the – unfortunately often very lucrative – business model for cyber attacks, according to the latest Cybercrime Report 2022 from the Federal Ministry for the Interior (BMI). It is a virtual danger that can cause real damage on a major scale. The number of reported cybercrime offences has been increasing at almost double-digit rates for years, with more than five times as many now compared with 2018. Geopolitical tensions have further exacerbated cyber threats, and cyber attacks are increasingly becoming an instrument of hybrid warfare. Attacks on critical infrastructure are another growth area. IT outages, especially prolonged ones, could trigger shocks on the financial markets and shake confidence in the financial system.

The FMA has therefore made IT security and cybersecurity of the supervised entities a strategic supervisory focus. In general terms, this relates to the protection of information and communication systems against damage and threats, from individual files to computers, networks and cloud services to data centres, regardless of whether the threat is an internal one or from outside the company. Cybersecurity measures should protect critical structures and sensitive information in networked systems from digital attack.

The FMA therefore carries out cyber maturity assessments to determine and evaluate the relevant risk awareness of the individual financial service providers, what preparations they have already made, and what still needs to be done. On-site inspections also focus on ICT security and cybersecurity. Business continuity management is a particular focus here. The FMA has also developed a blackout assessment, which has already been carried out at insurance undertakings and *Pensionskassen*. The results were generally positive, albeit with some potential for improvement also identified. This supervisory tool is now being rolled out to other supervisory areas.

Together with Oesterreichische Nationalbank (OeNB), the FMA is also conducting cyber stress tests for the Austrian financial market. Supported by Kompetenzzentrum Sicheres Österreich (KSÖ), the resilience of the financial sector to various cyber attacks is tested in a cyber simulation game scenario. As studies show that around two thirds of cyber damage is caused by employee error, the focus has been placed on the human factor. In particular, the cooperation between credit institutions and supervisory authorities as well as other institutions relevant to cybersecurity in the event of their systems being hacked was scrutinised.

The FMA also investigates how Austrian financial market participants are digitally networked with each other, with a focus on critical services outsourced to third-party providers such as data centres, cloud services or software providers and service providers. The resulting ICT service provider map highlights cluster risks, critical players, sensitive nodes and potential contagion channels. Identifying critical ICT service providers in Austria also helps to prepare for the EU's Digital Operational Resilience Act (DORA), which entered into force this year and will apply from the end of 2024.

The scope of DORA extends beyond financial service providers in the narrowest sense and also includes trading centres, providers of crypto services, insurance brokers and numerous other financial companies and even third-party providers in regulation and supervision. It set outs governance requirements for the procurement of critical ICT services and stipulates minimum requirements for the content of contracts between financial companies and ICT service providers. A new aspect here is the concept of a direct European supervisory regime, in which a European supervisory authority (EBA, EIOPA or ESMA) is assigned as the responsible supervisory body and then organises and coordinates the supervisory activities, including on-site inspections. DORA represents a standardised and coherent supervisory approach across the EU with the aim of ensuring that all financial institutions are able to maintain their operations even in the event of serious disruptions to their cybersecurity or information and communication technology. It sets out requirements for ICT risk management, establishes a reporting system for ICT incidents and significant cyber threats, requires digital operational resilience tests including threat-led penetration testing (TLPT) and includes provisions on obligatory information sharing as well as cyber crisis and emergency drills.

Digitalisation has also created a whole new world of financial services and assets in the form of virtual or crypto assets, a universe that has been expanding rapidly for years but is barely regulated. Moreover, as law enforcement is very difficult in the global, borderless realm of the internet, many dubious and even criminal providers are also active on these markets.

With the EU's Markets in Crypto-Assets Regulation (MiCAR), which will gradually become legally applicable from mid-2024, this world will be incorporated in a regulatory system for the first time. The aim is also to create a level playing field, i.e. fair competitive conditions in relation to strictly regulated analogue products and providers of financial services.

"The world of crypto assets has so far not been included in regulation and supervision. With the introduction of the Markets in Crypto-Assets Regulation, this is now gradually, but fundamentally, changing."

MiCAR makes a distinction between activities on the primary market, i.e. issuance of crypto assets, and services provided by the secondary market, or crypto-asset services. Specifically, it regulates transparency and disclosure obligations for the issuance and trading of crypto assets, the authorisation and supervision of crypto-asset service providers (CASPs) and issuers of crypto assets, the proper business organisation of crypto-asset issuers and crypto-asset service providers. MiCAR also includes investor and consumer protection regulations covering the issuance, trading and custody of crypto assets, as well as provisions to combat market abuse on trading venues.

The extent of the challenge facing the market and supervisors was already clear from the inclusion in 2022 of certain service providers of virtual currencies, known as virtual asset service providers (VASPs), in the regime for the prevention of money laundering. This is a relatively narrow field of regulation, and does not constitute a licensing process but merely registration. Notably, there is no prudential supervision. And yet this has completely overwhelmed many providers: of the 74 registration applications received, the FMA was only able to approve 32. Only 19 successful registrations were still valid by the middle of the year. Registration had to be withdrawn from all of the other providers due to failure to fulfil the legal obligations in practice or because the companies themselves opted to cancel their registration due to market failure.

MiCAR will play a key role in separating the wheat from the chaff in the market for digital assets.

THE FIGHT AGAINST GLOBAL WARMING

Human climate change is costing us all dearly. The European Commission found that climate-related events have been responsible for more than € 487 billion in financial losses in the EU over the past 40 years. More than 138 000 people died as a direct consequence of extreme weather and climate-related events in the EU between 1980 and 2020. The average economic costs of river flooding in Europe are more than € 5 billion a year, while losses of roughly € 2 billion can be attributed to wildfires.

To prevent a climate crisis, the global community reached the Paris Agreement in 2015, setting itself the goal of limiting global warming to a maximum of +2 degrees Celsius and subsequently bringing it down to +1.5 degrees. To reach this goal, EU Member States are required under the European Climate Law[1] to reduce their net

[1] *Regulation (EU) 2021/1119 of the European Parliament and of the Council of 30 June 2021 establishing the framework for achieving climate neutrality and amending Regulations (EC) No 401/2009 and (EU) 2018/1999.*

emissions of greenhouse gases by at least 55% by 2030 compared with 2019 levels. The EU wants to achieve its objective of complete climate-neutrality by 2050. Austria aims to be fully climate-neutral by 2040.These are ambitious goals, and they will only be achievable if our social and economic models are completely realigned towards more sustainability. The financial sector has a key role to play, since investments and financing decisions are having a major impact. Financial flows should be steered towards reducing climate risks. This means creating greater transparency around individual environmental risks in the real economy and the financial sector, enabling appropriate financial decision-making that favours sustainability. Climate-related risks are a major consideration for the economy and the financial markets even today, with greenhouse gas emissions and related issues increasingly turning from a risk to a cost factor. This is where regulators and supervisors need to step in.

Yet in view of the geopolitical and global economic realignment, as well as the looming economic recession, political priorities seem to be shifting right now, particularly in Europe: sustainability is slipping down the list of global priorities while global competition between different economic locations is gaining in importance.

The FMA is nevertheless unreservedly committed to the fight against climate change, prioritising support for the financial economy and financial markets as they transition towards a more sustainable economic model. After all, climate risks have the potential to create systemic risks in the financial sector. “Physical risks” such as natural disasters becoming more frequent and more extreme could cause enormous financial losses that could then also impact the financial markets. Likewise, transition risks, i.e. those that arise from the transition to a more climate-neutral and sustainable economic model, might have huge effects on financial service providers and financial markets. Specifically, because the financial markets might incorrectly assess and price climate risks in view of the long-term nature and huge uncertainties involved in transitioning.

Citizens, specifically investors, are very supportive of the fight against climate change, which is reflected in the developments on the asset management market: sustainable investment products have been booming for years. Just one example: of the approximately € 208 billion of assets managed in Austrian investment funds in mid-2023, almost € 90 billion, i.e. 40%, was held in funds with a sustainability focus in accordance with the Sustainable Finance Disclosure Regulation (SFDR[2]). Investors are clearly showing their commitment to more sustainability.

However, the asset management example is also indicative of the difficulties that still need to be overcome on the way towards more sustainability. A year ago, some 10% of these sustainability funds were regarded as “dark green” funds (Article 9 SFDR), while 90% were labelled as “light green” (Article 8 SFDR). Article-9 funds pursue sustainability in investment, for example by working towards ensuring that the United Nations’ Sustainable Development Goals (SDGs) are adhered to and by openly showing positive sustainability impacts. Article-8 funds only consider environmental and

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[2] *Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector.*

social aspects when selecting issuers to include in a portfolio. Currently, only about 3% of all sustainability funds are still defined as dark green, with 97% merely labelled as light green.

The reason for this lies in the fact that the criteria for labelling funds as light or dark green have been specified in greater detail, which triggered fears of reputational and liability risks. One of the points criticised was that major energy companies are among the largest investors in renewable and sustainable energy and related technologies. However, their core business is generally still fossil fuels. Another point: how to classify nuclear energy and natural gas as bridging technologies? The Taxonomy Regulation created a system of classification to facilitate environmentally sustainable investment. However, a lot of the detail still has to be fleshed out and the process is still a work in progress.

In general, the financial industry is very much aware of the importance of tackling climate change, and of its own involvement in these efforts. All our assessments at financial service providers have confirmed that they know that ESG (environmental, social and governance) factors need to be taken into account. However, there is still a lot of practical work to be done in applying that knowledge, which our climate stress tests at banks, insurance undertakings and *Pensionskassen* have shown.

The FMA was the first European supervisory authority to raise awareness of ESG risks within the financial sector when it published its Guide for Managing Sustainability Risks in 2020. The Guide illustrates how these risks, as well as having a negative influence on the performance of individual assets or financial market participants, can potentially also affect the stability of the financial market as a whole. It is intended to provide supervised companies with guidance on how to incorporate sustainability risks into their business activities, while also preparing them for regulatory developments and requirements. Accordingly, the Guide should be understood as a “living document” that is regularly updated.

The Guide also explains, by citing examples of best practice, how sustainability risks can be incorporated into existing risk categories, into strategies and corporate governance, as well as into any given transparency obligations. The related SFDR has been fully applicable since this year. It requires companies to disclose information regarding approaches to the integration of sustainability risks on their websites, and to include a description of the integration of sustainability risks as well as any adverse impacts in the pre-contractual information provided for each financial product. The Corporate Sustainability Reporting Directive (CSRD[3]) obliges all large undertakings and all listed undertakings, except micro undertakings, to provide information on the risks and opportunities resulting from social and environmental matters, as well as the impact of their activities on people and the environment. It must be applied for the first time to the 2024 financial year, and to reports for publication in 2025.

The challenge lies in specifying in detail what should qualify as sustainable, in a manner that is measurable, quantifiable and assessable. To this end, an appropriate reporting regime also needs to be established in the real economy. Supervisors, in

[3] *Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting.*

“Austria’s goal of being climate-neutral by 2040 is highly ambitious, and will only be doable if its social and economic models are completely realigned towards more sustainability. It is up to the financial market to steer monetary flows in this direction.”

turn, need to compile a broad base of data in order to be able to analyse and classify the gathered data, facts and figures. Quite a bit of creativity is still needed here, since big data, machine learning, data engineering, artificial intelligence and all manner of other technologies will have to be employed. The FMA analyses prospectuses in terms of sustainability versus greenwashing with the aid of AI. It matches its results with those of analysts and uses this as the basis for risk-oriented inspections. There are still many technological opportunities, and regulators and supervisors have a lot of hard work ahead of them.

The road to a sustainable business model will be long and rocky, and the financial sector and supervisors will have to tackle many major challenges along the way.

THE NEW ETHICAL IMPERATIVE

The growing significance of ethics and new values in our social interactions is also increasingly penetrating the financial markets. Society is making more and more demands for ethical and exemplary behaviour, and there is also a willingness to impose strict and consistent sanctions if the required standards are not upheld. While bribes were once tax-deductible, while aiding and abetting money laundering or tax evasion used to be a business model of highly specialised financial service providers, and the rules of cooperation in companies and markets were dominated by power structures and networks with no objective justification, such conduct is frowned upon today and consistently opposed. The fight against money laundering, terrorist financing and corruption is top of the agenda in the regulation and supervision of financial markets. Even a whiff of scandal, and the resulting reputational damage could easily threaten a company’s existence: no respectable financial service provider wants to be associated with dirty profiteers. In addition, appropriate corporate governance is no longer something that can be opted into. It is a strict regulatory obligation that can be enforced by supervisors. And ethical principles such as equality, diversity and inclusion are now part and parcel of our lives and workplaces.

Since the FMA was given the power more than ten years ago to monitor the efforts made by the supervised entities to prevent money laundering and terrorist financing, it has pursued a consistent zero tolerance policy. The Authority clamps down on any breaches of the rules with harsh penalties. This approach has proved successful, as shown by the latest country evaluations by the Financial Action Task Force (FATF), the global standard setter, as well as the International Monetary Fund (IMF). The number of suspicious transaction reports received by the Financial Intelligence Unit (FIU) at the Criminal Intelligence Service Austria (BK) has been rising significantly for years, and this is less a sign of the rise in money laundering cases in the Austrian financial system but proof that the system of prevention is working. Our supervisory priorities over the last few years, including those relating to correspondent banking relationships, business relationships with offshore centres and back-to-back transactions, have proved to be effective.

"Weak governance, complacency in the fight against money laundering or violations of the sanction regime currently constitute serious operational risks. All of these might lead to exorbitant fines, and the resulting reputational damage may even threaten companies' continued existence."

The biggest challenge in the fight against money laundering continues to be the fact that AML efforts are organised nationally while money launderers operate across borders and even globally. Any cross-border cooperation between authorities is complicated and time-consuming, especially because of the different legal framework in each country. Supervision is coming up against its limits in this area.

The FMA therefore expressly welcomes the European Union's ambitious AML/CFT regulatory framework and strong commitment to fighting money launderers. The new legislation will tighten up and harmonise European rules, and establish a dedicated European Anti-Money Laundering Authority for the first time. The AMLA will rely on the network of national supervisors to function, and promote and strengthen cooperation among them. Equipped with all the necessary regulatory and supervisory powers, the AMLA, together with the supervisory authorities in the Member States, will be tasked with ensuring that the legal provisions are uniformly applied and with promoting cooperation with the national criminal authorities, the Financial Intelligence Units (FIUs). In this way, as an authority with a European perspective, it will elevate anti-money laundering efforts to a new level and assume a leading role in the protection of the European internal market's integrity.

The FMA, as the national competent authority within this new European supervisory regime, will represent Austria's interests, contribute its broad expertise and work in close collaboration with its partners in the network.

The sanctions imposed by the European Union on Russia as a consequence of Russia's war of aggression in Ukraine have thrown a light on the efficient and effective enforcement of such resolutions. It is obvious that there is tremendous synergy in the financial market where the supervision of compliance with AML provisions is concerned. In Austria, it is presently up to the OeNB to sanction banks, while all other financial market participants and involved parties are subject to supervision by the State Protection and Intelligence Directorate (DNS) based at the Federal Ministry for the Interior (BMI). As an integrated supervisory authority, the FMA appreciates the initiative to also have it entrusted with the powers related to monitoring all financial service providers' compliance with sanction regimes. This will increase synergies, boost efficiency and effectiveness and create a "governance competence centre" for the entire financial market in Austria.

CHANGED CONSUMER BEHAVIOUR

The persistently low interest rate environment and the digital transformation have significantly changed consumer and investor behaviour.

Younger investors in particular have discovered riskier forms of investment in their hunt for returns and switched up to the next risk category: from savings books to bonds, from bonds to shares, from shares to certificates and exchange traded funds (ETFs). More sustainable investments are also becoming increasingly popular with young and retail investors, which has rejuvenated the capital market too. The number of 18 to 24-year-olds has more than quadrupled within three years, and the group of 25 to 39-year-olds has roughly doubled. Digital tools such as online and mobile phone banking, trading apps, online and neo-brokers have all made it so much easier to access stock exchanges and securities trading.

In view of the unattractive returns in classic investment categories, many consumers have been lured into believing sensational claims of amazing profits, opting to invest in unregulated and unsupervised markets on the internet: in highly speculative crypto assets and virtual currencies or via digital trading platforms, without first checking whether providers are reputable or not. This has resulted in many of them losing huge amounts of money as they fell victim to fraudsters. The ever increasing number of reports of suspicious investment transactions is further proof of this negative trend.

Having been socialised in a low interest rate environment has increased investors' risk appetite, particularly among the younger generation. Very often this comes with a lack of financial literacy and investment experience. This in turn means that many investors make the mistakes typical of novices, such as insufficient diversification and excessively high trading intensity, with the former drastically elevating the risk, and the latter massively pushing up costs and eroding returns. In fact, riskier and more complex financial instruments require more financial knowledge and investment and trading experience, not less.

Meanwhile, execution-only business is increasingly replacing more advice-intensive business, particular in digital offerings. This requires higher financial education on the part of consumers too, so that they can make appropriate decisions to match their personal financial needs. The playful design of many online services, financial products and apps gamifies the whole process of investing. Bonus systems, parallel interaction via social media, digital gimmicks and prize draws turn investment into one big game. Generally speaking, online investments – and investments made on smartphones in particular – show a higher trading intensity, with small amounts being bought and sold in quick succession, which drives up costs and lowers the returns.

Furthermore, when it comes to investing online, the legally required investor protection information is often provided in the form of pop-up windows, again particularly on phones, which users find annoying and just click away in a matter of seconds. In other words, investors decide to do without important information, sometimes even waiving their rights as customers and consumers.

Many investors' decision to move into higher risk categories and the profound changes brought about by the novel digital offerings with their innovative and distinctive features pose huge challenges for collective consumer protection. New approaches and technical solutions need to be found to guarantee the accessibility of information and reinstate transparency, and also to protect young and inexperienced investors. The objective should be that consumers receive easy-to-understand, targeted information so that they can make educated and appropriate decisions based on their financial needs. To this end, any information must be tailored to the digital channels and media that they use. Digital investors should receive the same level of investor and consumer protection as users of analogue financial services – a huge challenge.

"Consumers may use the borderless internet globally, with the digital technologies inducing them to see everything as a game, so that they increasingly forget about the risks in their hunt for returns."

In its capacity as an independent and integrated supervisory authority for the Austrian financial market, the FMA is tasked with the early detection of potential vulnerabilities in the financial market and its participants. The FMA must act in a risk-oriented manner and identify weak points before they reach breaking point. And we do this, for example, by preparing an annual medium-term risk analysis. Our risk analysis for 2024–2028 shows that all financial market participants in Austria have huge and difficult challenges ahead of them over the next few years – as does the FMA as regulator and supervisor. We will address these challenges boldly, rapidly, stringently, independently, holistically and in a risk-oriented and forward-looking manner, joining forces with our partners in supervision. Our priorities for supervision and inspections for 2024, derived from this medium-term risk analysis, are described in detail in the following chapter.

CodeLength++;
return result;
/// <summary>
/// </summary>
public static void CreateSchema(SqlConnection connection)
using (var command = connection.CreateCommand())

PRIORITIES FOR SUPERVISON AND INSPECTIONS 2024

The FMA lives by the principle of transparency and maintains an open dialogue with all stakeholders, the market and the supervised entities. Publishing the Authority's priorities for supervision and inspections for the following year is an important element of this approach.

Based on its annual medium-term risk analysis, in which it identifies and analyses the particular challenges in the financial markets over the next five years, the FMA evaluates and revises its supervisory strategy and sets its supervisory and inspection priorities for the coming year. It publishes the results in its annual publication Facts and Figures, Trends and Strategies and on its website.

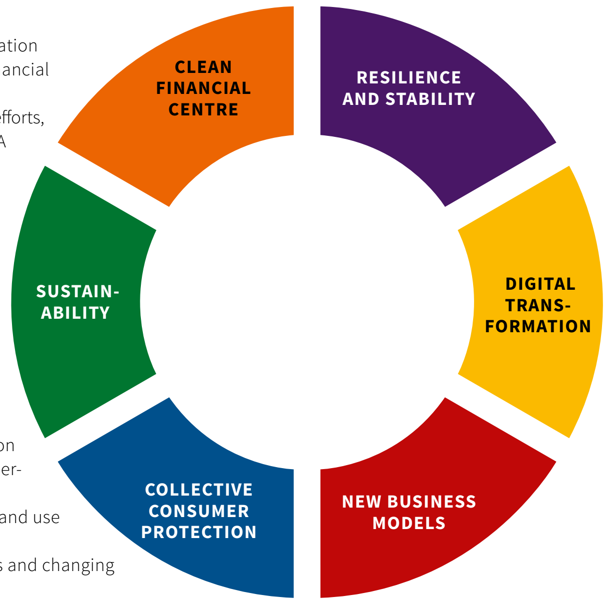
Using the Medium-term risk analysis and supervisory strategy 2024-2028, the FMA has defined and set the following priorities for supervision and inspections for 2024:

- **RESILIENCE AND STABILITY:** To strengthen the resilience of supervised financial service providers in times of crisis and preserve the stability of the Austrian financial market as a whole
- **DIGITAL TRANSFORMATION:** To exploit the opportunities of digitalisation while consistently addressing the associated risks
- **NEW BUSINESS MODELS:** To provide regulatory and supervisory support for innovative business models as early as possible in order to promote the innovative strength of the Austrian financial market, ensure fair competitive conditions and guarantee appropriate consumer protection
- **COLLECTIVE CONSUMER PROTECTION:** To further develop consumer protection in a rapidly changing environment focusing on digital transformation, changing consumer behaviour, demographic development, interest rate turnaround

Clean financial centre
- Accounting and reporting: correct presentation and quantification in financial and non-financial reporting
- Europeanisation of anti-money laundering efforts, further expansion into digital realm – AMLA
- FMA as governance competence centre – sanction regime

Sustainability
- Integration of climate and environmental risks in risk management, governance and strategy
- Transparency: focus on disclosures and non-financial reporting
- Greenwashing analysis in reporting and sustainability classification

Collective consumer protection
- Opening up new media and communication channels, targeted communication – cooperation with the OeNB
- Prevention of investment fraud – analysis and use of social media
- Market monitoring focused on digital sales and changing consumer behaviour



Resilience and stability
- Recognising, monitoring and addressing risks
- Improving capital resources and liquidity
- Strengthening corporate governance
- Prioritising property risks and the interest rate turnaround

Digital transformation
- Ensuring the stability of ICT systems – mapping
- Strengthening IT and cybersecurity – DORA
- Incorporating crypto assets into regulation and supervision – MiCAR

New business models
- Regulatory sandbox: focus on new providers under MiCAR
- Incorporating providers under MiCAR into supervision
- Creating a level playing field for analogue and digital providers

Figure 1: *FMA's supervision priorities for 2024*

- **SUSTAINABILITY:** To provide regulatory and supervisory support and assistance to the financial market and all its participants during the transition to a sustainable economic model
- **CLEAN FINANCIAL CENTRE AUSTRIA:** To secure the clean character and reputation of the Austrian financial centre at all levels.

Publication of the current medium-term risk analysis and the resulting supervisory and inspection priorities for the coming year is intended to draw the attention of the supervised entities to risk areas in their business field while also giving them the opportunity to prepare in a targeted way for the risk-oriented priorities for supervision in 2024. This raises awareness of risk and creates transparency around the challenges that the supervisory authority has identified and wishes to focus on. In this way, the supervised entities are also given a clear indication of which areas they should be focusing on.

PRIORITY FOR SUPERVISION AND INSPECTIONS: RESILIENCE AND STABILITY

The Austrian economy and the participants on its financial markets have coped well so far with the major challenges thrown up by the multiple crises of recent years: the COVID-19 pandemic, the huge economic upheaval caused by Russia's war against Ukraine, the crisis of multilateralism and the realignment of global economic flows, the repeated commodity and material bottlenecks as a result of the turmoil, the enormous surge in inflation forcing the central banks into an abrupt monetary policy turnaround, and a good deal other factors too. Despite all of the adversity, financial service providers and financial markets have proven to be stable and resilient, despite the inevitable volatility.

This is not least because regulatory and supervisory lessons have been learned from the global financial crisis of 2007/2008: regulatory gaps have been closed, existing regulations have been further developed in the light of experience and also harmonised across the EU, the supervisory architecture has been set in an European framework, new supervisory instruments have been created, and providers' capital base and liquidity have been significantly improved.

However, there has been no let-up in the geopolitical, real and financial challenges: inflation remains stubbornly high, particularly in Austria, the significant rise in interest rates is dampening the economy, global trade is slowing down and fears of recession are spreading worldwide. The huge rise in interest rates is making it considerably more expensive for consumers and companies, as well as the government, to borrow. This in turn hampers its fiscal room for manoeuvre when it comes to counteracting shocks. Given the sharp rise in borrowing costs, a consolidation of government spending is also inevitable in the medium term, which could further dampen economic output. And in addition to Russia's ongoing war of aggression against Ukraine, the terrorist attack by Hamas on Israel has inflamed another military flashpoint in a geopolitically sensitive region, further exacerbating global tensions.

This toxic mix has the potential to have a massive impact on the financial markets, increasing the risks in many areas and consequently also the vulnerability of the financial system. In the coming year, the FMA will therefore continue its supervisory focus on strengthening the resilience and crisis resistance of the Austrian financial centre, which it has consistently pursued for years. To this end, it will focus in particular on the following priorities and projects in 2024:

- **Identifying and closely monitoring risks, and targeted action to address vulnerabilities:** In view of the major challenges described above and created by the toxic mix of these geopolitical, real and financial developments, high volatility is to be expected on the markets with a corresponding impact on the financial market players. This means that forward-looking supervisory work including the identification and addressing of vulnerabilities at micro and macro level is crucially important. In addition to the effects of inflation, the focus will be on the
  - interest rate risk
  - credit risk and
  - liquidity risk

  facing companies. Furthermore, the focus on excessive developments in the property sector – both commercial and residential real estate – will be continued and taken further. Themed stress tests will also be carried out for all of these different challenges.
- **Strengthening corporate governance:** Strong and solid governance is the basis for coping with challenging times. Governance as a whole, and the key functions and their interaction with each other, can be further improved and strengthened by means of
  - fit & proper tests
  - deep dives
  - theme-based analysis of priorities and
  - the continuation of a structured dialogue with businesses.
- **Integrating new investment firms into the supervisory and resolution regime:** The entry into force and national applicability of the new supervisory regime for investment firms (IFD[1]/IFR[2]) has meant the introduction of a new class of investment firms. In order to ensure their smooth integration into ongoing supervision and the resolution regime (including the establishment of a separate national resolution fund managed by the FMA), this will be a key priority in the coming year.
- **Intensifying the review of credit institutions' resolvability:** Banks' resolution strategies and plans are now subject to more stringent reality checks. This means that, in addition to ongoing off-site analysis, they are subject to realistic tests and actual/target comparisons. One focus will be on the testing of management information systems (MIS) in the event of resolution.

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[1] *Investment Firms Directive: Directive (EU) 2019/2034 of the European Parliament and of the Council of 27 November 2019 on the prudential supervision of investment firms and amending Directives 2002/87/EC, 2009/65/EC, 2011/61/EU, 2013/36/EU, 2014/59/EU and 2014/65/EU.*

[2] *Investment Firms Regulation: Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms.*

DATA REQUIREMENTS IN RESOLUTION – FMA MINIMUM STANDARDS AND TECHNICAL IMPLEMENTATION

Experience with failing banks in the past has highlighted the importance of access to up-to-date and accurate data as the basis for appropriate and informed decision-making on restructuring and resolution. The Austrian Financial Market Authority (FMA) focuses on two aspects in relation to data requirements in the preparation of resolution cases: time and quality. If a bank looks likely to fail, decisions usually have to be reached at short notice, but it is nevertheless of vital importance to comprehensively evaluate all legal and economic aspects first. And this need for quality also extends to the quality of data. The challenge in such circumstances lies in obtaining and assessing high-quality data within a very short time so that it can be used as the basis for sound decision-making on the resolution, the resolution strategy and the applicable tools, thereby securing the future of a bank in crisis.

Against this background, the FMA has started to prepare a plan on how to obtain the required up-to-date data from banks as quickly as possible in the event of resolution. Following consultation with banks and auditors, the FMA laid down guidelines relating to the data requirements in resolution cases and published them in January 2021 in the form of FMA Minimum Standards on the provision of data in the event of resolution.

DATA MODEL

The FMA has been working with two expert partners, the Oesterreichische Nationalbank (OeNB) and the Austrian Reporting Services GmbH (AuRep), which are both well-versed in all regulatory reporting issues in Austria. Together, the three partners developed a data model to implement the FMA Minimum Standards. The biggest challenge in this regard was the issue of proportionality: to reconcile the requirements mentioned above with the possibilities of individual institutions.

The new model is based on the data model used in reporting, in which quality-assured data from the banks' data warehouses is fed into the OeNB's basic cube via the Integrated Reporting Data Model (Abacus/GMP) in a fully automated process. To make optimum use of the existing infrastructure, the data model was expanded to cover the new requirements set forth in the Minimum Standard by integrating those data points from the Minimum Standard into the model. The decision was made to implement the model-based approach instead of the more broadly used template-based approach for two substantial and decisive reasons: the high level of automation and AuRep's more than 100 000 standardised data quality checks.

This decision represents a milestone for data requirements in the event of resolution and ranks as a flagship project – even within the European Banking Union. It ensures that the two key challenges in banking resolution, i.e. time and quality, will also be addressed in the best possible way in terms of available data. The banks are able to reliably provide the required data in the desired frequency due to the high level of automation, while the data model ensures the same high quality as is customary in reporting.

SYNERGIES

The relational data model guarantees data integrity, which means the data is consistent across different points in time and also for any given point in time. Within the basic cube, complex relationships between data points are resolved, with the focus on ensuring that the data is unique and redundancy-free. This enables optimised data processing and efficient and reliable data management, which is reflected in the synergies. The Minimum Standards draw on existing data points from regulatory reporting, and the newly defined data points in the Minimum Standards are already being used for the data points required by the Single Resolution Board (SRB Bail-in Data Set and SRB Valuation Data Set).

Predefined data objects (entities) are generated from regulatory reporting and delivered to the defined target structure. Automated delivery makes it possible to store data in a virtual data room (VDR) of the bank, so that data is immediately available to the FMA in the event of resolution and related request for data provision. After the data is loaded from the VDR into the FMA's internal systems, it is carefully analysed and assessed by us. We can thus quickly provide the basis for sound and timely decision-making, paving the way for a successful resolution of the bank.

PRIORITY FOR SUPERVISION AND INSPECTIONS: DIGITAL TRANSFORMATION

Digitalisation is advancing at a rapid pace in business and society, and electronic tools are now being used in practically every area of our lives. New technologies such as machine learning, artificial intelligence and the latest hype surrounding large language models such as ChatGPT are only adding to the speed of this digital transformation. These are developments with a particular impact on the financial markets and all their players, bringing with them new opportunities but also harbouring new risks that should not be underestimated. Technological progress offers plenty of scope for innovative financial products, alternative forms of distribution and a modernisation of relationships with customers. However, digitalisation also offers established (analogue) companies a wide range of opportunities to optimise their business processes and become more efficient.

The FMA's goal here is to provide a regulatory and supervisory framework that facilitates and promotes innovation while at the same time upholding fair competitive conditions and appropriate consumer protection.

The FMA has been closely monitoring developments for years, with in-depth analysis of the changes and consistent action to address identified risks. Recent cyber maturity assessments, cloud assessments and IT security audits have shown progress and improvements across the market, but also a significant need to catch up in some areas. This applies not only to existing (analogue) providers, but also to new market players and digital business models. Structural changes in the market and the various interdependencies and concentration risks are another very relevant aspect in this regard.

In addition to the risks to financial market stability and to individual providers, the

FMA monitors the risks arising from product design, distribution and the provision of information to customers. One of its objectives is to ensure that the algorithms being used are not discriminatory. Despite all the euphoria about digitalisation, a door to the analogue world must always remain open so that population groups that lack digital skills are not excluded from the new developments or even from the financial market and essential services altogether.

All of this dynamic upheaval poses great challenges for market participants and supervisors alike. Dealing with these often means having to cooperate with or outsource to third parties. From a systemic perspective, this in turn can lead to new dependencies, risk concentrations and contagion channels. Supervision must therefore look beyond the financial market, include other regulated but also non-regulated activities and companies in its analysis, and find ways and means to address localised risks in a targeted, efficient and effective way.

The FMA will therefore be addressing the digital transformation in 2024 through the following projects and measures:

- **Survey on the status of digitalisation on the Austrian financial market:** The FMA has already conducted comprehensive digitalisation studies on the Austrian financial market, doing so in 2019 and 2021. A further cross-sector survey will be conducted in 2024, which will then be used to derive an Austrian Digital Finance Landscape. The aim of this comprehensive digitalisation map is to:
  - Determine the current level of digitalisation in companies in the various financial sectors
  - Provide an overview of the IT landscape at the supervised companies
  - Recognise interdependencies with other market participants in information and communication technology
  - Show how the supervised companies have developed since 2019.
- **Strengthening the digital operational resilience of companies and the financial market:** Once again in 2024 the FMA will continue to focus on the digital operational resilience of market participants and analyse their development. This will involve:
  - Assessing and updating the maturity levels of supervised institutions in their management of cyber risks (Cyber Maturity Level Assessments)
  - Progressing the roll-out of the FMA's cyber exercises designed to review companies' cyber resilience
  - Carrying out a cloud assessment for all sectors
  - Evaluating the impact of artificial intelligence applications on business models and business processes and incorporating this into the risk assessment
  - Focusing supervisory activities on the impact of artificial intelligence on market stability (e.g. through herding or threshold effects)
  - Focusing on IT security during on-site inspections.
- **Digital Operational Resilience Act (DORA)[1]:** With effect from 17 January 2025, the Regulation on digital operational resilience for the financial sector, including the

[1] *Regulation (EU) 2022/2554 of the European Parliament and of the Council of 14 December 2022 on digital operational resilience for the financial sector and amending Regulations (EC) No 1060/2009, (EU) No 648/2012, (EU) No 600/2014, (EU) No 909/2014 and (EU) 2016/1011.*

associated Level 2 and Level 3 measures, will apply in Austria. DORA comprehensively addresses and harmonises the risks associated with the information and communication technologies (ICT) used by financial companies with the aim of ensuring their operational resilience and stability. It also covers third-party ICT providers that are categorised as critical in its scope and in supervisory activity. Relevant financial service providers and third-party ICT providers will be required to comply with numerous digital security and reporting obligations in order to make financial service providers more resilient to cyber attacks and mitigate other risks from the use of ICT. In order to successfully fulfil these tasks, the FMA will increasingly be using new technologies, the selection and implementation of which will be supported and promoted by the FMA's internal Innovation Lab. To prepare for DORA, the FMA will:

- Set up an internal competence centre for the consistent application of the new European regulations across all sectors
- Systematically record third-party ICT providers and categorise them according to criticality
- Evaluate new SupTech applications for the FMA and implement them in the interest of efficient digitalised supervisory activities (VERBA, the database for consumer complaints and enquiries, and analysis relating to the fund sector and for capital market prospectuses, for example, are to be further automated using artificial intelligence)
- Create the organisational and technical requirements for incident reporting
- Continue to develop the audit programmes.

THE FMA CYBER EXERCISE

The threat posed by cyber risks continues to rise sharply. According to the Criminal Intelligence Service Austria's Cybercrime Report 2022, the number of cybercrime cases reported in Austria has more than doubled, up from 28 434 in 2019 to 60 195 in 2022. This equates to a 30.4% rise compared with 2021.[1] The latest cybersecurity study by auditing firm KPMG, based on survey data from 903 Austrian companies, shows a 201% increase in cyber attacks in the space of a year.[2] Meanwhile, the Allianz Risk Barometer 2023[3] and the World Economic Forum's Global Risk Report 2023[4] currently rank cyber risks among the top risks. Professional cyber risk management is therefore becoming increasingly important to businesses, especially in the financial market.

Austria's Financial Market Authority (FMA) has therefore been focusing on "digital transformation" as a supervisory and inspection priority for many years in order to promote the stability of digital systems and build resilience in the face of cyber risks.[5] It has developed a range of different supervisory tools since 2019 to analyse, review and strengthen cybersecurity. These now take the form of the FMA Cyber Security Toolbox, currently encompassing the following in particular:

- **Cyber Maturity Level Assessment:** The FMA has been using this self-developed tool to measure and evaluate cyber resilience since 2019.
- **Cloud Maturity Level Assessment:** The FMA developed this tool in 2019 to evaluate

[1] *Federal Ministry for the Interior/Criminal Intelligence Service Austria,* Cybercrime Report 2022 – Lagebericht über die Entwicklung von Cybercrime [Report on the development of cybercrime]*, May 2023, 22.*
[2] *KPMG, Security Forum Digital Economy Austria,* Cybersecurity in Österreich [Cybersecurity in Austria]*, May 2023, 9.*
[3] *Allianz Global Corporate & Speciality,* Allianz Risk Barometer*, January 2023, 4.*
[4] *World Economic Forum,* The Global Risks Report 2023*, 18th edition, January 2023, 6.*
[5] *FMA, Facts and Figures,* Trends and Strategies 2023*, 20 et seq.*

the precautionary measures taken by insurance undertakings and *Pensionskassen* when using the cloud.

- **Blackout assessment:** The tool is used to analyse the extent to which businesses have considered the potential implications of a blackout on their day-to-day operations, as well as their business conduct rules and risk coverage.
- **Assessment of migration measures:** The aim is to evaluate the security measures (mitigations & detections) that the supervised entities have taken to tackle a current cyber attack scenario (selected by the FMA).
- **Cyber exercise:** While the previous assessments ask structured questions about the existence of strategies, processes and security measures, the cyber exercise puts the companies' cyber preparations to the test in a realistic manner. Based on a realistic simulation of a cyber attack, the FMA evaluates the appropriateness of the reactions of the participating insurance companies to the injects (information describing what is happening, such as emails, phone calls, tweets, messages) in real time.

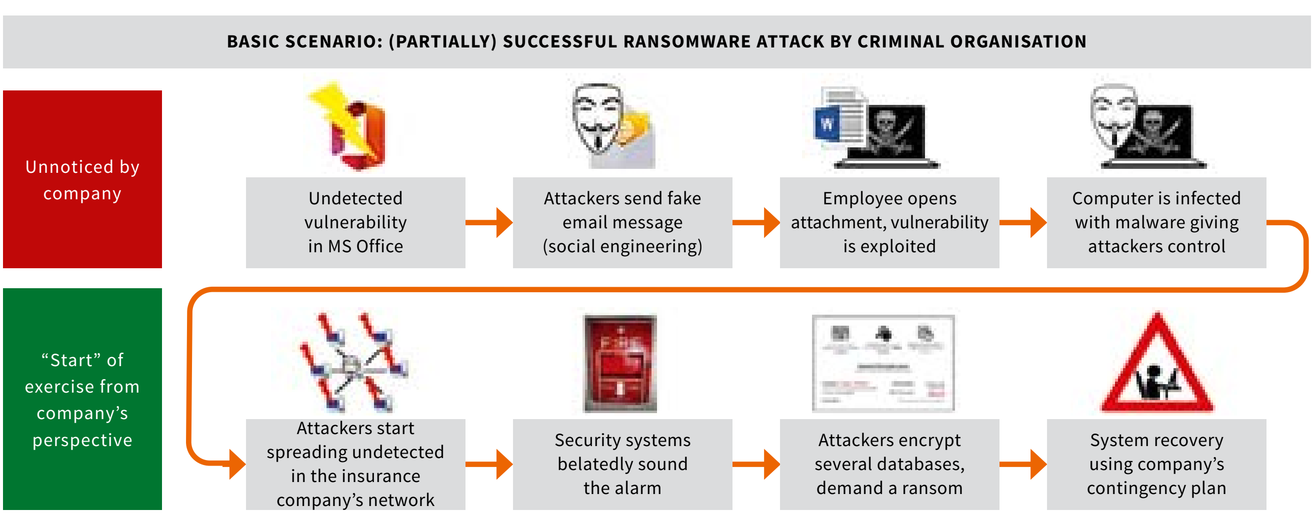
CYBER EXERCISE – A REAL-TIME TEST

In order to make the cyber exercise as practice-oriented as possible, the FMA draws on findings from its supervisory priorities, and uses external sources such as the ENISA Threat Landscape[6] of the European Union Agency for Cybersecurity or the MITRE ATT&CK®[7] knowledge database created by The MITRE Corporation.

In 2023, a phishing-based double-extortion attack, namely an extortion attempt based on both the theft and the encryption of sensitive data, was selected as the basis for the exercise *(> Figure 1)*. The MITRE ATT&CK® matrices were used to specify the attack steps at a technical level, as these illustrate the processes involved in real-life extortion attempts.

The cyber exercise involves the FMA team simulating a cyber attack by emailing the participants tailored information fragments (injects) about a hypothetical, ongoing cyber attack against the company *(> Figure 2)*. The FMA team then also monitors how

Figure 1: *Rough outline of the attack scenario (source: FMA)*



[6] *European Union Agency for Cybersecurity,* ENISA Threat Landscape 2022, *October 2022.*
[7] *The MITRE Corporation,* MITRE ATT&CK®.

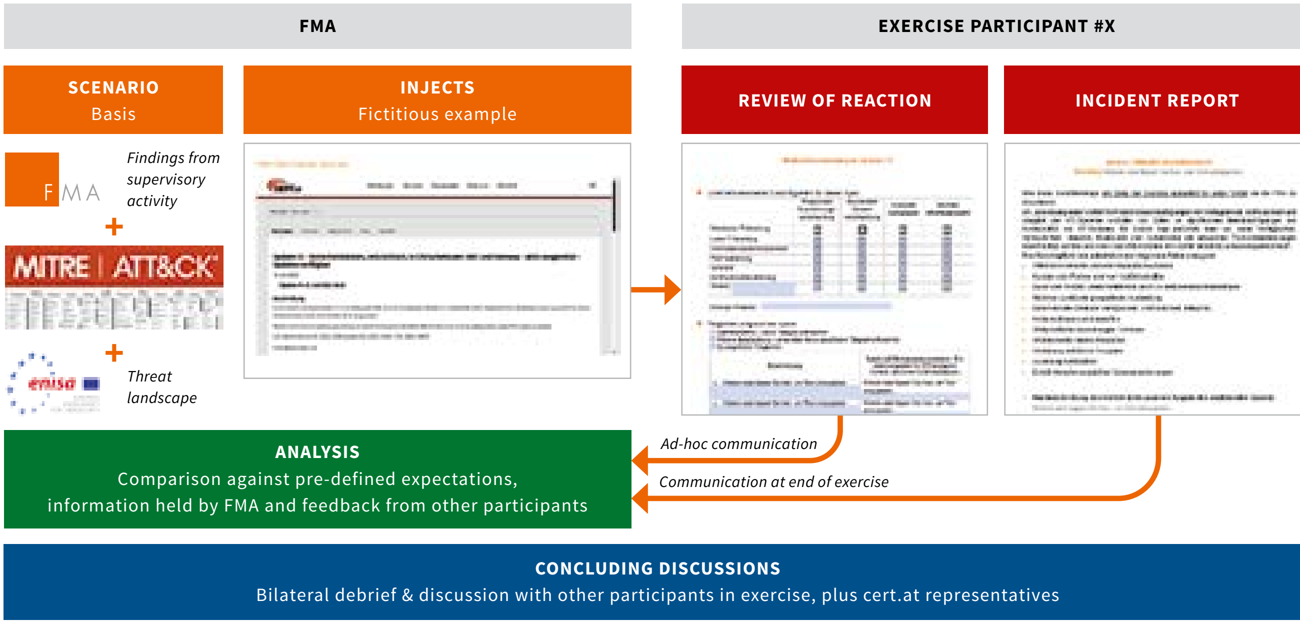


Figure 2: *Outline of the FMA cyber exercise process (source: FMA)*

the affected company's emergency team respond to the fictitious attack, and can also be contacted if urgent questions arise.

The task of the participating companies is to analyse these injects and define appropriate responses to each in order to protect and secure its information and communication technology (ICT) within a very tight timeframe. At the end of the exercise, ICT incident reports must be created, which are subsequently analysed and reviewed.

The FMA then compares the reactions of the participating companies with previously defined expectations and with the information already available on the respective participant (e.g. from the FMA Cyber Maturity Level Assessment and the assessment of mitigation measures). During a debrief, the results of the analysis are discussed bilaterally with the participants and any measures for the further development of cyber resilience are also covered.

Finally, the companies have the chance in a follow-up meeting to discuss the reactions of the other participants and to analyse the results with representatives from cert.at, thereby learning from other companies' good practices.

The FMA cyber exercise is intended to help the participating companies to better understand the potential impact of simulated cyber attacks, to question the appropriateness of their individual approach, to initiate any further improvements to their own cyber resilience and to prepare for the Regulation on digital operational resilience for the financial sector (DORA Regulation[8]), applicable with effect from January 2025.

[8] *The Digital Operational Resilience Act (DORA) entered into force on 16 January 2023.*

PRIORITY FOR SUPERVISION AND INSPECTIONS: NEW BUSINESS MODELS

Economic and social changes are transforming the business models of many supervised companies and prompting new market players with innovative business models to enter the market. The supervisory priority of "new business models" has already been heavily influenced by the emergence of technology-driven business models in recent years.

The FMA has taken these developments into account in the past and acted in accordance with the existing body of rules. In the meantime, the European legislator has focussed on identifying the relevant technological developments and recording them under supervisory law as part of a targeted Digital Finance Strategy, while also addressing the opportunities and risks with new regulatory framework conditions. With the introduction of the DLT Pilot Regime[1], it has already created a simplified supervisory framework for investment firms, market operators and central securities depositories that want to trade and settle tokenised securities on the regulated market. This has created the regulatory basis for the fast, efficient and low-cost trading of security tokens (tokenised assets as programmable assets) on regulated markets in the EU. The year 2024 will be characterised by the gradual implementation and application of the Markets in Crypto-Assets Regulation (MiCAR)[2], which will mean numerous new regulatory requirements for market participants and practitioners in the

[1] Regulation (EU) 2022/858 of the European Parliament and of the Council of 30 May 2022 on a pilot scheme for market infrastructures based on distributed ledger technology, and amending Regulations (EU) No 600/2014 and (EU) No 909/2014 and Directive 2014/65/EU.

[2] Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937, OJL 150, 9 June 2023.

crypto economy. Some articles of the Regulation have been applicable since its entry into force on 29 June 2023, the provisions on ARTs and EMTs will essentially apply from 30 June 2024, and all other provisions take effect from 30 December 2024.
The supervisory priority for 2024 is therefore dominated by internal preparations for the FMA's expected responsibilities[3] in connection with MiCAR:

- **Implementation of MiCAR – conceptual design and internal organisational structure:** The expected powers and tasks of the FMA within the framework of MiCAR are diverse and range from authorisation procedures, answering legal questions, representing Austrian interests in international working groups to numerous activities as part of ongoing supervision. A core aspect of the FMA-wide preparations for MiCAR is the establishment of a supervisory structure for the authorisation and ongoing supervision of crypto-asset service providers (CASPs), issuers of asset-referenced tokens (ARTs) and electronic money tokens (EMTs), the monitoring of white papers, and preparing for market monitoring and market abuse prosecution. To this end, the FMA will be focusing on the following areas in 2024:
  - Definition and integration of the structural and procedural organisation for MiCAR
  - Preparation of authorisation and ongoing supervision of CASPs, issuers of ARTs and issuers of EMTs
  - Evaluation of the use of artificial intelligence to review and analyse white papers for crypto assets that are not ARTs or EMTs
  - Design and preparation of internal processes for market monitoring and market abuse detection, taking into account the scope of the institutions to be supervised.
- **Connecting factors to MiCAR for existing and new business models:** In accordance with its integrated supervisory approach, the FMA will identify, analyse and record under supervisory law potential connecting factors to MiCAR in relation to banks, FinTech enquiries, the operation of the regulatory sandbox, and the prevention of money laundering and terrorist financing. In particular, the FMA will examine whether supervised institutions or newly interested licence applicants offer MiCAR business models. In this context, the FMA will carry out the following measures:
  - Dialogue with credit institutions planning to sell services and products relating to crypto assets to retail clients
  - Analysis and consideration of conduct and governance issues in MiCAR implementation
  - Monitoring of market developments in crypto assets, as well as integrated assessment of new business models and development of structures to consistently combat unauthorised providers with regard to MiCAR implementation
  - MiCAR-related consumer information and communication
  - Identification of potential, innovative business models for the further development of the regulatory sandbox, taking particular account of the new opportunities presented by MiCAR, and monitoring of market developments
  - FinTech Navigator update to take account of MiCAR

[3] *At the time of writing, the FMA had not been appointed by the legislator as the competent supervisory authority nor entrusted with any other powers in connection with MiCAR.*

- Monitoring and analysis, as well as networking and targeted coordination with European partner authorities with regard to applications from cross-border VASPs/CASPs in order to prevent regulatory arbitrage and to consistently develop the FMA's zero tolerance policy in the crypto sector
- Analysis of money laundering and terrorist financing risks in cooperation models between the traditional financial sector and the crypto sector.

MICAR – AN EU-WIDE APPROACH TO REGULATING CRYPTO ASSETS

Digitalisation continues to advance steadily and continuously. It increasingly touches our day-to-day lives, transforming many areas of our lives in the process. As well as changing the needs of consumers, this digital transformation is also impacting the needs of companies, with new business models emerging as a result. Innovation is booming: new digital tools and solutions such as distributed ledger technology (DLT), platform economies, artificial intelligence (AI), machine learning and the metaverse are increasingly gaining a foothold in the financial markets too, a place where digitalisation is advancing particularly rapidly. Innovative ideas are being brought together, and new business models are evolving. Innovation is "contagious": one innovation inspires another or helps it to develop. Many of the resulting new business models enable connectivity across borders, and many of them can be and are already being offered globally.

Vast areas of these new business models based on new digital inventions have so far escaped regulation, which was originally geared towards the analogue world, and this is particularly true of virtual assets, or crypto assets. To tackle this inequality, certain providers of virtual currencies were included in the scope of the Financial Markets Anti-Money Laundering Act (FM-GwG; *Finanzmarkt-Geldwäschegesetz*) as a first step, and obliged to adhere to due diligence obligations to prevent money laundering and the financing of terrorism. However, some EU Member States have adopted divergent implementation laws at national level. There has been no Union-wide regulation aimed at ensuring investor protection, and the integrity and stability of the financial market. Some Member States, such as France or Malta, introduced specific regulations for services related to crypto assets, but these only applied nationally. All of this has resulted in a fragmented European market as far as crypto assets are concerned, and with no legal security, their further development is being hindered.

From mid-2024 however, the Markets in Crypto-Assets Regulation (MiCAR)[1], which entered into force on 29 June 2023, will be gradually applicable throughout the European Union (EU): it will apply to stablecoins (ARTs[2] and EMTs[3]) from 30 June 2024, and then all remaining further provisions in MiCAR will take full effect from 30 December 2024. In particular, the MiCAR lays down transparency and disclosure requirements for the issuance and trading of crypto assets, requirements for the authorisation and supervision of crypto-asset service providers (CASPs) and issuers of crypto assets, as well as their orderly business organisation; requirements for the protection of investors and consumers in the issuance, trading and custody of crypto assets; and provisions to combat market abuse on trading platforms for crypto assets. The new regulation differentiates between activities on the primary market, i.e. issuance of crypto assets, and services provided by the secondary market, or crypto-asset services.

The MiCAR aims to create a harmonised European regulatory framework for any offer to the public, admission to trading and provision of services in connection with crypto assets within the EU. It promotes innovation and the utilisation of the potential of crypto assets while at the same time safeguarding financial market stability and these markets' integrity, offering a high degree of investor protection.

The new regulatory obligations laid down in MiCAR include a number of additional competences and powers that will be conferred on the FMA. To be well prepared for the challenges ahead, the FMA aims to:

- Obtain an overview of the range of potential (new) supervised entities early on
- Evaluate possibly necessary internal changes in its organisational structure
- Expand its knowledge in terms of technical, economic and supervisory market developments in a targeted way

and create the necessary requirements to fulfil its obligations. To support financial innovation in Austria, the FMA encourages interested market participants to contact it with any enquiries before the MiCAR actually becomes applicable, helping to provide legal and planning security. In addition, the FMA is actively engaged in all European and international bodies to secure the interests of the Austrian market and its participants.

[1] Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto assets, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937, OJ L 150, 9 June 2023.

[2] Asset-referenced token.

[3] Electronic money token.


+24.19%
+16.00%
+7.87%
285,300
23,800
154,500
100
100
Volume

PRIORITY FOR SUPERVISION AND INSPECTIONS: COLLECTIVE CONSUMER PROTECTION

Driven by digitalisation, big data and artificial intelligence, the financial and capital markets are experiencing a period of profound change. Financial innovations and digital distribution make it quicker and easier for consumers to participate in the financial and capital markets. While this opens up new benefits and opportunities, there are also disadvantages and risks to consider.

It is younger generations, digital natives, who are making the greatest use of the tempting and diverse possibilities of the electronic financial wonderland, with online and mobile phone banking, online brokers, neo-brokers and platform economies also changing user behaviour. The style of messages is short and snappy. Automated comparisons tend to be biased. Media use is constant, and access often playful. The pop-ups containing important information required by law to protect consumers are often just perceived as annoying, and can be clicked away in a fraction of a second. Transparency is lost in the blaze of information. Meanwhile, the rapid advance of digitalisation is increasingly pushing back analogue offerings, branch sales and advice-intensive business. This means that those customers who are less confident with digital technology or unwilling to engage with it are increasingly being cut off from the market and the chance to meet their basic financial needs.

Moreover, growing digitalisation and an internet with no international borders are leaving digital wallets and accounts exposed to online scams and fraudulent financial offers. Financial fraud is booming, with the number of enquiries, complaints and reports to the FMA increasing every year.

These are trends that pose major challenges for collective consumer protection.

The FMA's goal is to provide consumers with straightforward information that has been

tailored to the target audience, enabling them to make informed decisions in line with their financial needs. Given the pace of digital change, there are some areas in which supervisors also need to break new ground. Consumer protection must be refocused; objective, non-sales-driven information needs to be made available in an even more targeted way, and increasingly designed around digital information channels.
To this end, the FMA will implement the following projects and measures in 2024:

- **Insurance distribution:** Compliance with the legal requirements for internal product development and product approval procedures for insurance investment products will be a supervisory priority. By applying the requirements of the European Insurance and Occupational Pensions Authority (EIOPA)[1], we ensure that the insurance investment products developed meet the needs of the target market, namely that they take into account the objectives, interests and characteristics of customers and avoid negative effects for them. On-site audits are also carried out on topics relating to insurance distribution and to product oversight and governance (POG), and the supervisors' expectations regarding the internal organisation of POG requirements for insurance investment products are communicated.
- **Prevention of investment fraud:** Given the persistent and massive increase in investment fraud, the FMA is strengthening its target group-oriented consumer information and moving into new media channels. This includes cooperation arrangements with the Oesterreichische Nationalbank (OeNB) and the evaluation of a joint approach with various different stakeholders.
- **Market monitoring with the focus on digital distribution:** Market monitoring is being expanded with a focus on the younger nature of the capital market and the associated risks. A special focus will be placed on digital sales and online platforms. In particular, a deep-dive analysis will be used to compare the age groups and their investment behaviour in order to determine the different risks (such as a lack of diversification or increased trading activities) that exist between them.
- **Conduct focus on rights and obligations when using payment services:** Consumer protection authorities, the European Banking Authority (EBA) and the FMA are increasingly taking notice of phishing and social engineering fraud. As part of its remit under the Payment Services Act (ZaDiG 2018; *Zahlungsdienstegesetz*), the FMA will therefore be focusing on compliance with the obligations placed on credit institutions in relation to transaction monitoring/transaction risk analysis and customer information. As a first step, it will work on obtaining a market overview of the transaction monitoring mechanisms[2] and customer information of selected credit institutions. The FMA will then discuss anomalies and supervisory expectations as well as best practices with the market in order to raise market standards in fraud prevention.

[1] *EIOPA Methodology to assess value for money in the unit-linked market, EIOPA-BOS-22/482.*
[2] *Article 2 of Commission Delegated Regulation (EU) 2018/389.*

DIGITAL FINANCIAL TRANSACTIONS VIA SMARTPHONES – A CHALLENGE FOR CONSUMER PROTECTION

The influx of younger generations into the capital market, which has gained considerable momentum during the pandemic, shows no sign of letting up. At the same time, digital financial services are increasingly being accessed via smartphones, and thus via the online platforms of banks and investment service providers, and via neo-brokers and trading apps.

This poses a major challenge for collective consumer and investor protection, as digital providers primarily operate on an execution-only basis. Consequently, investors are required to assume a much greater degree of personal responsibility in the absence of any advice or recommendation from an advisor, not to mention any expert assessment of the suitability or appropriateness of the investment service. For young and inexperienced investors in particular, there is a danger that the risks typically associated with a financial product, such as issuer risk and liquidity risk, will not be recognised or understood.

Additionally, with execution-only transactions, investors should be carefully considering their own investment knowledge and experience, their financial circumstances, their investment objectives, their risk strategy, their own ability to bear risk and losses, and whether the transaction is in line with their investment objectives.

Consumers often find the pop-up windows containing the investor protection information that must be provided by law before a contract is concluded annoying and will just click them away without a second thought. This is hardly surprising since, according to a study, the average consumer would need 76 days to go through all the obligatory information in their existing contracts. As a result, many people simply tick the mandatory “I have read and understood” box without even having glanced at the information.

Studies also show that young investors with little financial education are particularly likely to consume investment and financial information on social media rather than anywhere else. However, social media sites will generally bring with them a strong influence and a higher potential for impulsive acts, triggering very fast and intensive trading activity online. Many trading apps are based around "gamification", using playful elements to make trading seem more appealing. It is common for the focus to be on gaming success, rewards and competitions, rather than on the particular financial product and whether or not it is suitable. Easy-to-understand user interfaces suggest that these are non-complex products, but this is often not the case.
Research into behavioural finance shows that investors frequently imitate the behaviour of the majority. In terms of market activity, this type of herd behaviour creates strong price and rate fluctuations due to similar patterns of trading activity. This is exacerbated by social media and online research.

SUPERVISION PRIORITY SOCIAL MEDIA MONITORING

As part of the expansion of risk-oriented market monitoring, the FMA will be establishing social media monitoring in relation to investment and financial recommendations and their links with providers of digital financial services in the coming year. The aim is to track information flows on the marketing, distribution and sale of financial instruments as the basis for positioning tailored information campaigns. By providing information, the FMA wants to help young investors in particular to critically scrutinise why they are drawn to a particular investment and why other investments are less appealing to them.
In addition, the FMA will also be analysing transaction data to identify and monitor financial market trends and risks, comparing the diversification of the portfolios of younger and older groups of investors in order to provide targeted information on the advantages of diversifying financial instruments and investment products. The holding period applicable to financial products from different asset classes will also be compared for the different investor age groups. The aim is to find out whether a lack of education and digital trading could lead to a lack of diversification and increased trading activity, since intensive activity on the markets results in higher costs overall, which in turn has a negative impact on returns.

PRIORITY FOR SUPERVISION AND INSPECTIONS: SUSTAINABILITY

The increasing intensity of extreme weather events illustrates the huge and devastating impact of climate change. By promoting the transition to a sustainable economy, the financial sector and the players within it can make a significant contribution to mitigating climate change and its consequences.

This applies not only at European level, through the European Green Deal, which aims to make the EU climate-neutral by 2050, but also at national level. Indeed, intensive work is continuing on achieving the climate targets that Austria has set for itself. For this reason, a cross-sector scenario analysis is to be carried out in 2024 under the leadership of the European Commission with the cooperation of the European Central Bank (ECB), the European Systemic Risk Board (ESRB), the European Supervisory Authorities (ESAs) and the national supervisory authorities. The resilience of the EU financial system will therefore also be assessed on the Austrian financial market, with the cooperation of the FMA, and findings will be gathered in connection with the transition to a low-carbon economy, including under stress conditions.

Within this priority for supervision and inspections, the FMA will therefore be focusing on the following projects:

- **Integration of climate and environmental risks in risk management, governance and strategy**: As part of the European Green Deal, the FMA and OeNB are actively involved in the 2024 scenario analysis, focussing on the Austrian market. In addition, climate stress tests are being carried out at national level across several sectors and industries. The climate scenarios used in these are based on those specified by the European Commission. Meanwhile, the review of the integration of sustainability risks into risk management, strategy and governance as part of the supervisory review and evaluation process (SREP) is one of the FMA's supervisory and inspection priorities. The results of the implementation check of the FMA Guide for Managing Sustainability Risks are taken into account. The further development of the Guide is intended to provide the supervised entities with a broad knowledge base of supervisory expectations, deepen existing expertise and promote a common understanding of the issues at stake.

- **More in-depth greenwashing analysis of sustainability transparency and dis closures:** Compliance with the regulatory requirements on sustainable finance and the associated transparency regulations will continue to be increasingly integrated into ongoing supervisory activities. This applies in particular to the implementation of the new requirements arising from the obligation to provide information on sustainability aspects in accordance with the Corporate Sustainability Reporting Directive (CSRD)[1]. An analysis and review of the existing reporting and disclosure requirements on sustainability in connection with the Taxonomy Regulation[2], in particular Article 8, will also be established. The disclosures in accordance with the Sustainable Finance Disclosure Regulation (SFDR[3]), the Taxonomy Regulation and the Non-Financial Reporting Directive (NFRD[5]) are designed to reduce the risk of greenwashing. In order to further reduce this risk, the fight against greenwashing in funds and sales is being prioritised. Convergent supervisory approaches and effective measures to prevent greenwashing will also be prioritised in insurance and pension supervision. The continuation of the inspection focus on sustainability in the sale of ESG financial products by banks is to be further developed.

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[1] *Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting.*

[2] *Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.*

[3] *Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector.*

[4] *Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.*

FMA CLIMATE STRESS TESTING 2024

Continued and increasingly extreme weather events are a stark reminder of the negative effects of climate change. The financial sector and its participants have a significant role to play in reaching the necessary climate goals and promoting the transition to a more sustainable economy.

The European Green Deal aims to transform the European Union (EU) into a climate-neutral continent by 2050. To achieve this target, the European Commission has asked the European Central Bank (ECB) and the European Systemic Risk Board (ESRB) to work together on a one-off scenario analysis exercise in 2024. In addition to the European institutions, the Austrian supervisory authority will also be working closely with the ECB on this exercise, which should assess the resilience of the financial sector in the EU in implementing the regulatory "Fit for 55"[1] package and determine the financial system's ability to support the transition to a low-carbon economy even under adverse stress scenarios. After the first climate stress test at EU level in 2022 focused on the long term and on transition and physical risks, the 2024 exercise will concentrate on transition risk and the energy sector, not least motivated by the energy crisis, and a shorter time horizon.

To this end, the Austrian Financial Market Authority (FMA) will conduct climate stress testing at Austrian insurance undertakings, *Pensionskassen* and investment funds in 2024.

The FMA has been carrying out stress testing in insurance and pension supervision

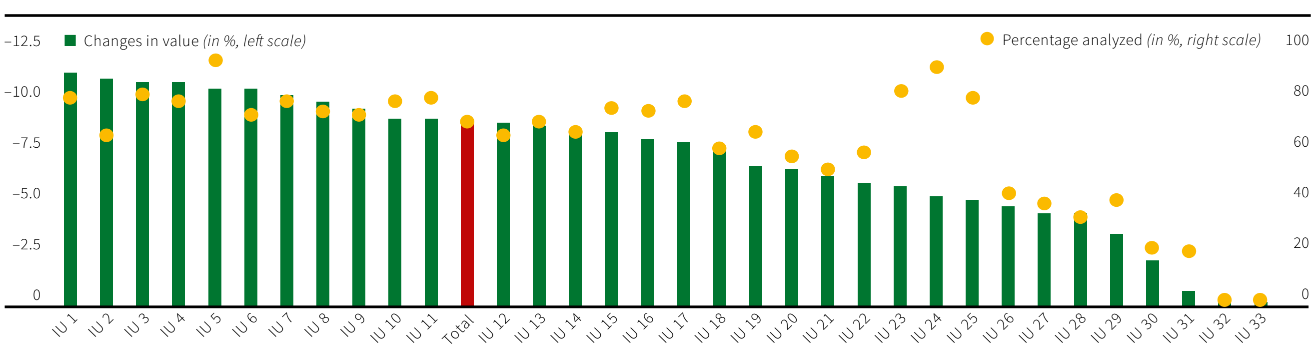
[1] *"Fit for 55" is a package of legislation consisting of amended as well as new Commission directives and regulations for delivering the EU's climate targets. The legislative package is based on the European Green Deal, which it is designed to implement. It was introduced on 14 July 2021.*

since 2019 to analyse prudential risks and vulnerabilities in the Austria provision market caused by environmental risks. The FMA is continuously working on improving its testing tool and, since it places great emphasis on granularity and automation, it conducts stress test calculations using proprietary R programming codes.

The current climate stress test model is based on a carbon price shock. It models a sudden increase in carbon prices triggered by a delay in the introduction of measures to reduce carbon emissions. The scenario used is based on the scenario assuming an orderly transition that was developed by the Network for Greening the Financial System (NGFS). This can be used to carry out analysis and calculations for shares and for government and corporate bonds. It assumes a price shock for shares and a yield shock in the case of bonds. Provided that all of the required parameters are available, the exact cash flow from the reporting date up to maturity can be presented. In this way, not only yield shocks but also yield curve shocks can be modelled using exact present value recalculations. Recalculating the present value is the preferred method. If any of the required parameters are missing, an estimate is made using a modified duration and convexity. As soon as the Fit-for-55 package's stress test scenarios are available, they will be incorporated into the existing structures.

The latest stress test found that the value of insurance undertakings' portfolios in relation to total exposure had declined for the overall market by around 8.6% in the fourth quarter of 2022, with around two thirds of the portfolio having been included in the analysis *(> Chart 1)*.

***Chart 1:** Effects of climate stress testing by insurance undertaking (Q4 2022, FMA representation)*

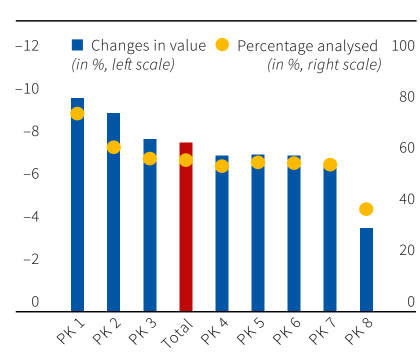


In the case of *Pensionskassen*, the result for the overall market was approximately –7.5% in the fourth quarter of 2022, again based on around two thirds of the portfolio *(> Chart 2)*.

***Chart 2:** Effects of climate stress testing by* Pensionskassen *(Q4 2022, FMA representation)*

The FMA analyses provide an overview of the developments and current status quo of investments in climate-related assets including their possible impact. We are continuously striving to improve how we present the results of our analysis work. For in-house purposes, we are using a dashboard developed by Power BI.

Both our analysis of insurance undertakings and *Pensionskassen* and our surveys of credit institutions have shown that supervised companies are increasingly focusing on sustainability issues.



PRIORITY FOR SUPERVISION AND INSPECTIONS: CLEAN FINANCIAL CENTRE

To ensure confidence in a financial market's proper functioning, and in its stability and ability to supply financial services to the real economy and consumers, it is essential for that market to be "clean". The digital transformation, global economic upheaval in the wake of armed conflicts, soaring inflation and the abrupt turnaround in interest rates, as well as changing consumer behaviour, are also bringing with them new and previously unfamiliar dubious business practices and types of product. Periods of great uncertainty and profound upheaval are also periods during which fraudulent providers and those engaged in criminal activity tend to fare best.

These dynamic and highly volatile developments not only have an impact on the risks and results of supervised companies and their business partners, but also bring major changes to the investor market. To take just one example: financial products are increasingly being sold via social media. These distribution channels are becoming ever more appealing to a younger audience with sometimes dubious advertising and sales practices, although the regulatory framework established to ensure the clean status of the capital market (including market abuse regulations) has not yet been enforced accordingly. The world of crypto assets is also only gradually being included in the scope of regulation. New technological approaches in particular are often very quickly misused for money laundering purposes, be it to develop new methods and techniques, or to take advantage of unsuspecting consumers (turning them into money mules).

There are also signs that the zero tolerance policy consistently pursued by the FMA in the fight against money laundering and terrorist financing (ML/TF) must be further expanded in an integrated way across sectors and borders. The imminent replacement of the existing AML/CFT regulations on certain virtual asset service providers (VASPs) by the new European MiCAR requires close networking and targeted coordination with our European partner authorities and the relevant EU institutions, particularly during the transition period. The aim must also be to prevent regulatory and supervisory arbitrage during this time. Due to new cooperation models between the traditional financial sector and the crypto sector, ML/TF risks must also be addressed at this interface. This will require the further development of data-based supervisory tools.

For all these reasons, the supervisory authority must monitor the markets particularly closely in order to quickly identify dubious business practices, dubious providers and fraudulent products, but also to efficiently address inappropriate sales and advertising practices. On this basis, the following priorities for supervision and inspections will be set for 2024:

- **Financial reporting:** In light of the multiple crises, geopolitical upheaval, and the real economic and financial challenges, a key focus must be placed on accurate presentation and quantification in financial and non-financial reporting.
- **Social media monitoring:** In the fight against market abuse, processes and systems for the ongoing relevant monitoring of social media have to be evaluated and put in place. This will involve developing implementation concepts and carrying out feasibility analysis.
- **Transparency rules:** As part of ongoing market monitoring, particular attention is paid to Austrian bond issuers' compliance with the regulatory requirements in terms of transparency (ad hoc disclosure and directors' dealings) and compliance with the Market Abuse Regulation (MAR[1], insider lists and trading bans). To this end, investigations are conducted on an ad hoc basis and compliance checks are carried out randomly with regard to blocking periods and insider lists.
- **Whistleblowing:** In order to manage the increase in whistleblower reports efficiently and effectively, IT solutions for recording whistleblower reports and monitoring the processes, measures and results must be evaluated and put in place. The results of the Court of Audit's report must be implemented and the processes under the Whistleblower Protection Act (HSchG; *HinweisgeberInnenschutzgesetz*) must be further developed in accordance with the interpretation of the Act by the relevant ministries.
- **Combating money laundering and terrorist financing:** The FMA's consistently applied zero tolerance policy must be taken further across all sectors, and the strict standard in the registration of VASPs must be transferred to the new regime under MiCAR. Awareness of the strict AML/CFT requirements must also be expanded in all regions and sectors. The inspection focus on particularly risk-prone transactions and the know-your-customer principle will be continued. Close cooperation with the Financial Intelligence Unit (FIU) at the Criminal Intelligence Service Austria and the public prosecutors will be intensified in order to be able to pursue complex

[1] *Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (Market Abuse Regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC.*

supervisory cases (on-site and off-site) efficiently and effectively. A further focus will be placed on new approaches to group supervision. During the transition period for the application of MiCAR, monitoring, analysis, networking and targeted coordination with European partner authorities will be strengthened in relation to applications from cross-border VASPs/CASPs in order to prevent regulatory arbitrage and consistently uphold the policy of zero tolerance in the crypto sector. The structured dialogue with supervised entities and stakeholders will be expanded in order to actively and specifically communicate the FMA's expectations for the prevention of money laundering and terrorist financing.

- **Preparations for the EU's new AML/CFT regulatory framework:** The aim is to position the FMA as the national anti-money laundering supervisory authority for the financial market in the future structure of the newly created EU Anti-Money Laundering Authority (AMLA), which will rely on the network of national supervisors to function.
- **Assumption of supervisory powers in sanctions law:** Preparation for the gradual assumption of supervisory powers in relation to sanctions law, powers currently still held by the OeNB.
- **Further development of FMA policies:**
  - Evaluation of the European Securities and Markets Authority's heat map for the prioritisation of administrative penalty proceedings and the opportunity policy.
  - The assessment of penalties when conducting ML/TF proceedings must be evaluated in light of the recommendations[2] of the EBA, which also has powers in the fight against money laundering.
  - The FMA policy on the conduct of proceedings relating to individual offences in the fight against money laundering and terrorist financing must be evaluated and, if necessary, further developed in accordance with the current decisions of the Supreme Administrative Court (VwGH).

[2] *EBA AML implementation review.*

COMBATING MONEY LAUNDERING – FINANCIAL SUPERVISORS' STRATEGIC USE OF BLOCKCHAIN ANALYSIS TOOLS

The highly specific innovative technologies behind crypto assets and virtual currencies mean that they pose an elevated risk of being misused for money laundering and terrorist financing (ML/TF). To counter this risk, legislation to prevent money laundering and terrorist financing in connection with crypto assets is being expanded. Certain providers in relation to virtual currencies, the virtual asset service providers (VASPs), have been subject to the regime of the Financial Markets Anti-Money Laundering Act (FM-GwG; *Finanzmarkt-Geldwäschegesetz*), which transposes the Fifth Anti-Money Laundering Directive[1] into national law, since 10 January 2020. In 2024, the new Transfer of Funds Regulation[2] will enter into force, which will significantly enhance ML/TF prevention and improve the traceability of crypto transactions in particular.

The Regulation is based on the more broadly defined term of crypto-asset service providers (CASPs) pursuant to the Markets in Crypto-Assets Regulation (MiCAR)[3]. The term comprises the following services:

- Providing custody and administration of crypto assets on behalf of third parties
- Operation of a trading platform for crypto assets
- Exchange of crypto assets for fiat currencies

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1 Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36/EU.

2 Regulation (EU) 2023/1113 of the European Parliament and of the Council of 31 May 2023 on information accompanying transfers of funds and certain crypto-assets and amending Directive (EU) 2015/849.

3 Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937, OJ L 150, 9 June 2023.

- Exchange of crypto assets for other crypto assets
- Execution of orders for crypto assets on behalf of third parties
- Placing of crypto assets
- Providing transfer services for crypto assets on behalf of third parties
- Reception and transmission of orders for crypto assets on behalf of third parties
- Providing advice on crypto assets
- Providing portfolio and asset management for crypto assets

Or simply put, wallet provision, exchange and trading services.

In accordance with the recommendations of the Financial Action Task Force (FATF), the international standard setter for AML/CFT, the new Transfer of Funds Regulation widens the Travel Rule to include crypto-asset service providers. This means that CASPs that are transferring virtual assets from or to another CASP on behalf of a client also need to transmit, obtain and save material information on the sender and the recipient, specifically names, addresses and account numbers of both the sending and receiving client.

This marks an important step towards more transparent and traceable crypto transactions, making it easier for the FMA to implement its strict zero tolerance policy in the fight against money laundering, which it has consistently applied across all sectors.

DATA-BASED ANALYSIS TOOLS

Both financial service providers and supervisory authorities are increasingly using blockchain analysis tools for the efficient and effective identification and evaluation of money laundering risk within crypto transactions. From the supervisors' point of view, it is not just a question of monitoring individual transactions effectively but also of recognising ML/TF risks and trends early on. Even though the European Banking Authority (EBA) is still working on its guidelines, the supervisory authorities are imposing more and more AML/CFT requirements and expectations on CASPs in relation to the ongoing and automated monitoring of client transactions. Technical aspects, the unique nature of crypto-asset services and its impact on the relevant control mechanisms all have to be considered in this context.

A RISK-BASED AND TECHNOLOGY-NEUTRAL APPROACH TO SUPERVISION

In its capacity as competent supervisory authority for financial service providers that are active in the Austrian market and therefore subject to the FM-GwG, the FMA was quick to recognise the relevance of innovative blockchain analysis tools in ML/TF prevention and has integrated it into its own data analysis system. To tackle the growing and many new challenges in the rapid crypto world, the FMA is continuously optimising its existing supervisory tools, also developing new applications in close cooperation with academia.

For instance, in a pilot project based on transaction data, it is working on a risk profile of crypto-asset service providers in the Austrian financial market. The objective is to include blockchain analysis both in inspection activities and official investigations, and in risk analysis. This way, ML/TF risks should be identified at an early stage at both the micro and the macro level, enabling a focused use of supervisory resources for combating money laundering and the financing of terrorism.


FIT FOR FUTURE

THE FMA'S NEW SUPTECH TOOLS – MILESTONES ON THE ROAD TO DATA-DRIVEN SUPERVISION

In its role as a regulator and supervisor, the Austrian Financial Market Authority (FMA) must quickly identify new developments and challenges before addressing them efficiently and effectively. To do this, it must also question itself from time to time, considering its objectives, values, organisational structure, working methods and tools. With this in mind, it launched its "Fit for Future – FMA 2025" transformation programme in 2021, which uses a medium-term risk analysis to determine the success factors of regulation and supervision for the future. The aim is not merely to react to new developments, but to be a transformative authority that always has its finger on the pulse and actively shapes new topics from the start. This is to be achieved through a flexible organisational set-up, modern technical equipment and infrastructure, and highly qualified staff who are motivated to take on the challenge. One of the specific objectives is to address the challenges of digitalisation and ensure that data is being used optimally.

The FMA is therefore consistently pursuing a forward-looking and successful path towards data-driven supervision. Its ambitious goal is to analyse the valuable data sets using state-of-the-art technologies in a way that means risks are identified and tackled even more quickly. The tools and work processes of the supervisory authority are also being continuously optimised in order to pursue the goals of financial market stability and sustainable confidence in the proper functioning of the financial market in the best possible way, even in the midst of a rapidly changing market environment.

To this end, the FMA is reviewing its entire working environment in order to reorganise it in a future-oriented and flexible manner. The aim is not only to scrutinise and overhaul existing structures, but also to create a culture of innovation. Numerous innovative tools are already thriving in this inspiring environment, with our employees integrating them into their work processes on a daily basis. Here we provide an initial insight into some of these innovations.

VUSA

One of these projects, known as VUSA (which stands for solvency analysis of insurance undertakings in German), has the ambitious goal of modelling changes in the solvency of Austrian insurance companies as a function of external capital market factors. The innovative technology, which is categorised as nowcasting, can support insurance supervision not just on a day-to-day basis but also in terms of reacting to crisis situations. When it comes to accurately and quickly assessing the stability of companies, this technology provides specific indications of potential threat scenarios and risk areas, thus improving the information base for sound decision-making.

AML/CFT[1] APPLICATION

In the fight against money laundering and terrorist financing, the FMA has recently started using an integrative AML/CFT application that gives employees a 360-degree view of supervised companies. Automated links present all of the relevant information, from key financial figures to risk factors, in a clear and interactive format. This not only increases the efficiency of the FMA's work, but also improves its understanding of the supervised companies.

VERBA TOOL

In the area of collective consumer protection, the FMA has developed an innovative tool, VERBA (which stands for consumer, complaint and enquiry in German), to process complaints and enquiries efficiently. By analysing data with the help of artificial intelligence and implementing an integrated workflow, anomalies and trends can be identified at an early stage, which helps to protect consumers even more effectively than before.

All of these projects and tools pursue common goals, namely to analyse supervised companies more comprehensively, to simplify our workflows and to identify risks on the financial markets earlier and more clearly in order to implement the FMA's statutory remit more quickly and efficiently.
Through its "Fit For Future – FMA 2025" transformation programme, the FMA is creating the spaces and structures, such as its recently developed Innovation Lab, in which ideas and innovative projects can be implemented accordingly.

[1] *Anti-Money Laundering/Combating the Financing of Terrorism.*