Growing Asia's Markets

15 December 2016

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Monetary Authority of Singapore
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By e-mail: hsho@mas.gov.sg, liquidity@mas.gov.sg

Dear Ms. Ho,

Re: Consultation Paper on Local Implementation of Basel III Liquidity Rules – Net Stable Funding Ratio (NSFR) and NSFR Disclosure

The Asia Securities Industry and Financial Markets Association (ASIFMA)[1] and its members support the underlying policy goals of the Net Stable Funding Ratio (NSFR), including its core objective of requiring banks to develop and maintain sustainable funding structures.

So we appreciate the Monetary Authority of Singapore's (MAS) efforts to ensure that its draft guidelines are consistent with the Basel Committee on Banking Supervision's (BCBS) final standard, and welcome the opportunity to respond to the MAS's "Consultation Paper on Local Implementation of Basel III Liquidity Rules -- Net Stable Funding Ratio and NSFR Disclosure" (Consultation Paper). We support the MAS's proposals for its domestic implementation of the NSFR.

As the MAS considers how to implement this global standard in Singapore, we encourage it to examine the impact of the final NSFR on Singapore's economy and, as one of Asia's financial centres, on Asia's economic development. Notwithstanding our support for the MAS's proposal and, more broadly, the NSFR's underlying goals, we have general concerns about the BCBS's standard and its treatment of repo and interlinked transactions. These elements of the proposed NSFR stand to reduce capital market activity and increase costs for end-users and investors.[2]

ASIFMA, through its umbrella organisation -- the Global Financial Markets Association (GFMA), has conveyed to the BCBS its reservations on the NSFR standard and its impact on capital markets. In responses to European Commission and US agency consultations on local implementation of NSFR submitted in the summer of 2016, we and our trade association partners (the Association of Financial

[1] ASIFMA is an independent, regional trade association with over 80 member firms comprising a diverse range of leading financial institutions from both the buy and sell side, including banks, asset managers, law firms and market infrastructure service providers. Together, we harness the shared interests of the financial industry to promote the development of liquid, deep and broad capital markets in Asia. ASIFMA advocates stable, innovative, competitive and efficient Asian capital markets that are necessary to support the region's economic growth. We drive consensus, advocate solutions and effect change around key issues through the collective strength and clarity of one industry voice. Our many initiatives include consultations with regulators and exchanges, development of uniform industry standards, advocacy for enhanced markets through policy papers, and lowering the cost of doing business in the region. Through the GFMA alliance with SIFMA in the United States and AFME in Europe, ASIFMA also provides insights on global best practices and standards to benefit the region.

[2] Oliver Wyman study, "Impact of NSFR on capital markets," January 2015.

Markets in Europe [AFME][3] and the Securities Industry and Financial Markets Association [SIFMA] [4] in the United States as well as the GFMA) have highlighted how the NSFR raises costs for end-users, and reduces liquidity in financial markets. Those effects will likely be amplified in Asia's developing financial markets.

Any evaluation of NSFR's impact must consider how banks allocate regulatory capital, funding and liquidity costs internally, as required by BCBS standards. Although exact practices vary by institution, as a general principle banks evaluate internal business units' profitability against all applicable prudential standards. If capital markets activities in Asia are subject to unrealistic NSFR treatments, every business line within an Asian capital markets franchise – whether at a traditional investment bank or a more retail-focused institution – will be evaluated against the implied regulatory funding costs of operating those businesses.

In addition, banks operating globally are especially cognisant of the need to be rigorous about allocating and minimising costs – limiting the ability of even an NSFR-surplus bank to subsidise the funding costs of a capital markets franchise with, for example, retail division Available Stable Funding (ASF) surpluses.

While end-users may or may not be able and willing to absorb incremental cost increases in capital markets services – which cannot be the prudential objective of the NSFR – we believe the larger effect on financial markets will be lower activity and greater volatility. This is an especially pressing concern for developing markets in the Asia-Pacific, which are less deep and less liquid, than those in the US or Europe.

Notwithstanding these broader concerns with the global NSFR standard, ASIFMA supports the MAS's approach but would appreciate further clarity around the scope of its proposal. We would also like to highlight ways we believe the treatment of repurchase agreements and interdependent assets and liabilities could reduce the impact of the NSFR on Singapore's capital markets.

Scope and application

We support the MAS's approach in applying the NSFR only to domestic systemically important banks (D-SIBs). We also welcome proposed lower NSFR requirements for D-SIBs whose groups are not headquartered in Singapore to take into consideration the fact that funding is generally managed at group level. However, we seek clarity on Article 4.4 regarding the circumstances under which "MAS could, on a case by case basis, increase the all-currency NSFR requirement of these banks."

Treatment of repurchase agreements

ASIFMA recommends that further consideration be given to the ASF and Required Stable Funding (RSF) factors assigned to repurchase agreement (or "repo") transactions under the proposed framework.

Repo transactions play a vital role in the financial system and underpin the functioning of primary and secondary capital markets as well as short-term money markets. The development of a "classic" repo market is an important step for deepening financial markets in Asia. Deep, liquid repo markets encourage

[3] Association of Financial Markets in Europe, International Swaps and Derivatives Association and Institute of International Finance, Response to European Commission consultation paper "On Further Considerations for the Implementation of the NSFR in the EU," https://www2.isda.org/attachment/ODQ3OQ==/AFME-ISDA-IIF%20EC%20NSFR%20Response.pdf

[4] The Clearing House Association, the Securities Industry and Financial Markets Association, the Financial Services Roundtable, the American Bankers Association, the Institute of International Bankers and the CRE Finance Council, Response to Multiple Agencies' "Notice of Proposed Rulemaking – Net Stable Funding Ratio: Liquidity Risk Measurement Standards and Disclosure Requirements," http://www.sifma.org/comment-letters/2016/sifma-and-other-associations-submit-comments-to-multiple-agencies-on-net-stable-funding-ratio/

the establishment of a benchmark yield curve – an important step for price certainty and transparency in the capital markets. They foster the proliferation of more experienced broker-dealers and market makers, and stimulate the development of hedging tools, which contribute to better risk management. Indeed, the MAS recognised the importance of deep, liquid repo markets when it launched the Securities Repo Facility in 2015. In a 17 November speech at the ASIFMA Annual Conference in Singapore, MAS Deputy Managing Director Jacqueline Loh said: the "[MAS is] also engaging investors, issuers and intermediaries to assess if more can be done to facilitate an active repo market and whether this will help deepen liquidity in bond markets."[5]

However, the adoption of the current NSFR proposal based on the BCBS standard could therefore run counter to the MAS's goal of developing a deeper, more liquid bond market in Singapore, as well as deeper markets throughout Asia. Small asymmetries in ASF and RSF factors (e.g. 10-15%),[6] as specified in the MAS's consultation, would raise costs for what is already a high-volume, low-margin business that is already shrinking due to the impact of the leverage ratio, and may be contributing to a decline in market liquidity.[7]

We understand that the asymmetry between the ASF and RSF factors is designed to penalise bank interaction with the unregulated financial sector, including hedge funds. However, we note that the BCBS has provided no evidence or guidance as to what the right amount of interaction may be, or how the proposed asymmetry in the NSFR would achieve it. The proposed treatments under the NSFR are therefore particularly disproportionate and at risk of unintended consequences.[8]

The European Commission (EC) is already taking steps to reduce the impact NSFR stands to have through the repo market on Europe's economic growth and reduce the unintended consequences on end-users. On 23 November, it published legislative proposals revising its Capital Requirements Regulation and Directive (CRR/CRD IV).[9] The NSFR is a key component of that legislative package.

The EC proposed, for example, to set a 0% RSF on Level 1 high-quality liquid assets (HQLA), versus 5% under the BCBS standards. This treatment is consistent with the treatment of those assets under the existing Liquidity Coverage Ratio. The EC further proposed reducing the RSF of secured lending below what was proposed in the BCBS standard; in the EC's legislative proposal, the RSF on secured lending is 5% on Level 1 HQLA – versus 10% in the BCBS standard – and 10% on level 2A HQLA – versus 15% -- to preserve market efficiency given the central role of secured lending in the financial system.

We appreciate the EC's approach, but remain concerned that its changes are not sufficient in mitigating the NSFR's impact on the repo market. As an alternative to the current Basel Committee approach, ASIFMA urges global regulators to consider a similar approach to Level 1 HQLA to minimise the effects of implementing NSFR on government bond markets – particularly less-liquid markets in Asia – and less-

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[5] Jacqueline Loh, Deputy Managing Director, Monetary Authority of Singapore. "Strengthening Asia's Bond Markets," speech delivered 17 November at the Asia Securities Industry & Financial Markets Association's Annual Conference.

[6] For more information, please refer to page 13 in the International Capital Market Association, "Impact of the Net Stable Funding Ratio on Repo and Collateral Markets," March 2016, http://www.icmagroup.org/assets/documents/Regulatory/Repo/ERCC-NSFR-230316.pdf

[7] Global Financial Markets Association and International Institute of Finance, Response to IOSCO's Public Comment on Examination of Liquidity of the Secondary Corporate Bond Markets, October 2016.

[8] International Capital Market Association, "Impact of the Net Stable Funding Ratio on Repo and Collateral Markets," March 2016,

[9] European Commission, Proposals to amend rules on capital requirement, 23 November 2016, http://ec.europa.eu/finance/bank/regcapital/crr-crd-review/index_en.htm

developed repo markets. ASIFMA suggests that the asymmetry between ASF and RSF factors be eliminated, or re-proposed with analysis that supports how it might achieve the intended outcome. Another, less desirable, option would be to apply the asymmetry of ASF and RSF factors for repo transactions only to agreements with non-regulated financial entities.

Interdependent assets and liabilities

We appreciate that the MAS allows banks to allocate 0% RSF and 0% ASF when transactions meet all criteria for interdependent items. Without exempting specific capital markets activities, several aspects of the global NSFR framework will severely restrict banks' ability to facilitate client financing, investing and hedging – and thereby hinder capital markets' development and their ability to support economic growth.

The NSFR framework requires banks to use long-term funding for transactions that are already well-funded and short-term in nature, which would materially increase transaction costs without necessarily improving liquidity risk management. A range of interdependent transactions or pass-through facilitation trades would need to be funded -- often on long-term basis, materially increasing the cost of such transactions. These higher costs are likely to be passed on to investors and end-users.

ASIFMA proposes specific treatment for certain activities, including:

- Inter-company funding;
- Export financing;
- Derivatives hedges/initial margin;
- Clearing of client trades;
- Segregation and custody of customer assets; and
- Facilitation of client and firm short transactions.

These transactions support hedging, clearing and trading by long-term investors – activities that support the real economy. Globally, we have urged regulators to apply a neutral funding treatment to these capital markets activities so that banks are able to maintain market liquidity and continue offering clients efficient, tight pricing. This neutral treatment would help mitigate some of the adverse impacts of the NSFR standard while strengthening liquidity risk management among banks in Singapore.

We welcome the opportunity for continued engagement with the Monetary Authority of Singapore as it considers this important regulation. If you have further questions or would otherwise like to follow up, please contact Wayne Arnold, ASIFMA Executive Director and Head of Policy and Regulatory Affairs at warnold@asifma.org or +852 2531 6560.

Sincerely,

Mark Austen
CEO
Asia Securities Industry and Financial Markets Association