AMUNDI'S RESPONSE TO BCBS'S CONSULTATION ON

HAIRCUT FLOORS FOR NON-CENTRALLY CLEARED SECURITIES FINANCING TRANSACTIONS

(January 5th, 2016)

Amundi is the leading asset manager in Europe and ranks in the top 10 of the industry worldwide, with assets under management above € 950 billion at the end of September 2015. Located at the heart of the main investment regions in more than 30 countries, Amundi offers a comprehensive range of products covering all asset classes and major currencies. Amundi has developed savings solutions to meet the needs of more than 100 million retail clients worldwide and designs innovative, high-performing products which are tailored specifically to the requirements and risk profile of institutional and corporate clients.

Amundi is a listed company with Credit Agricole Group as its majority shareholder. For prudential regulation purpose, Amundi is integrated within Credit Agricole Group and subject to minimum capital requirements on the concerned activities. As an asset manager, Amundi trades, on behalf of the funds and clients, large amounts of Repos and reverse repos and in securities lending and borrowing. The main counterparties are investment banks selected on the basis of their financial strength and low risk profile as well as for their presence on the market and specifically prices offered and liquidity provided. We do appreciate the new opportunity BCBS offers stakeholders to express views on the proposed framework for minimal haircuts on securities financing transactions (SFT). Actually, we believe that more attention should be paid to funds and the asset management industry when designing the new rules.

The consultation document asks the following two questions.
Q1. Are there any weaknesses or further improvements to the proposals that the Committee should consider?
Q2. Are there any specific implementation challenges with the proposals?

Amundi understands the objectives of the regulation as recalled in the document :

- "Limit the build-up of excessive leverage",
- "Create incentives for banks to set their collateral haircuts above the floors rather than hold more capital",
- "maintaining incentives for market participants to conduct their own analysis of the appropriate level of haircuts",
- Favour central clearing .

We globally share them but realize that they do not all apply to asset management and funds.

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Keeping these objectives in mind, Amundi would like to present the following comments.

1. **Regulation and prudential regulation:**

We know that asset management is a key actor on market finance and can be as such suspected, at first sight, of threatening the financial stability and operating as shadow banks. Further analysis should evidence that the risk does not rely with the asset management industry which is highly regulated. European Asset managers as well as their funds are subject to specific directives (AIFM, UCITS), they are required to closely monitor risks and are under strict supervision of competent authorities. Asset managers are not subject to prudential regulation for the basic reason that they operate funds in which investors have put capital. Asset managers act as pure agents for their clients. They do not carry any significant engagement nor investment on their own balance sheet. They manage assets for the client investors who have entrusted them with their subscriptions and take very seriously their fiduciary duty towards these client investors.

Let's say that we feel that market finance includes many very different situations. Some institutions do operate like banks without being properly supervised. Asset management is on the contrary a tightly regulated and supervised industry that works on capital provided by clients and that does not develop hazardous investment strategies in the back of regulators. We provide transparent reporting and constantly act in the best interest of our client investors.

2. **Asset managers and SFTs:**

Asset management has developed Efficient Portfolio Management (EPM) with a view to increase the safety and/or the return for client investors. Regulators have turned EPM to SFT putting the focus on the banking side and away from the asset management activity. It appears that some clarification on the position of asset managers is needed. Let us explain. Typically funds are active on two types of trades:

- Reverse repo is frequently used as a safe way to invest cash with good financial conditions and high mitigation of the counterparty risk through the reception of collateral; on behalf of money market funds, Amundi trades 24 hour Reverse Repos in billions every day;
- Securities lending is mainly directed on specific shares or bonds where there is a market demand making it possible for fund holders to get a reasonable enhancement of the performance.

The other two types of transactions, direct repo and securities borrowing, are far more unusual. Except for a few funds, mainly hedge funds, that use leverage as part of their investment strategy, Repos will unfrequently be used to adjust liquidity on a very short term and within a strict limit, 10% of the NAV of the fund. Securities borrowing is of relevance for funds that may short stocks (straight or within an arbitrage strategy) and here again hedge funds are the only candidates to develop such strategies. We do not mention securities borrowing as part of the resolution process of a failed delivery which is both purely technical and temporary in essence.

Except for a limited number of hedge funds, asset managers acting on behalf of the funds they manage have not as primary motive to gain financing for the funds when they enter into a SFT. BCBS should consider an exemption for UCITS and AIF not using significant leverage.

3. Leverage build-up:

Investment funds are prevented from leveraging. For UCITS leverage is limited to 2 and, in practice, the same rule applies for AIFs that are offered to retail investors. In any case, AIFs who wish to exceed a leverage of 3, known in the regulation as AIFs using significant leverage, are subject to specific requirements in the field of risk control and extra reporting made available to the competent authority. Noteworthy, to underline that leverage in these regulations does not mean borrowing to reinvest or any other way to get cash in addition to capital provided by investors. No, leverage includes as well leverage obtained through derivatives when they add to the economic exposure of the fund. It is an extensive definition of leverage.

Consequently, UCITS and AIFs not using significant leverage are counterparties of SFTs that will not build up any leverage on their side. However, in a reverse repo we provide cash to counterparties who may well reinvest it and leverage their balance sheet.

4. Cash collateral reinvestment and collateral re-use:

On that chapter as well, funds regulation is very restrictive. Currently UCITS are totally forbidden to re-use any security received as collateral (SFTs are also prohibited) and they are limited when reinvesting cash collateral to a short list of eligible highly liquid, high quality assets such as treasuries and cash deposits with prime banks. The rule is not as drastic for AIFs. It is fortunate, as it allows exchange of collateral in order for a fund that does not hold eligible securities to access the derivative market and clear through a CCP. UCITS funds are denied that possibility and a high yield UCITS for example will not be able to properly cover its interest rate risk through listed futures because it does not hold eligible collateral. Its choice will be either to keep exposure or to reduce the total amount it invests (what dilutes the performance) and keep a specific cash buffer to meet initial and variation margin calls. Amundi thinks that some flexibility should be introduced for UCITS to solve this issue.

Following the introduction of the European SFT Regulation re-use will have to be explicitly approved by the provider of collateral, knowing that transfer of ownership implies consent to re-use. We consider that regulation as a real progress towards full transparency and better investor protection even if we see enhanced reporting of transactions as redundant with EMIR in many instances.

5. Eligible highly liquid assets:

Amundi shares the approach defined by BCBS high level principles under proposed article 143(xii). Asset managers do establish a policy on reinvestment of cash collateral for relevant funds. For UCITS the regulation itself lists eligible assets and introduces diversification rules. However, we believe that one should not confuse priorities. Risk on derivatives does not rely on collateral first. The risk stems from:

- The volatility of the underlying
- The leverage included in the derivative if any and more generally the structure of the derivative
- The financial situation of the counterparty
- The frequent valuation of the derivative and exchange of variation margin

- The existence of collateral
- The quality of the collateral.

We do agree that minimum haircutting is appropriate to enhance the stability of the financial system. It participates to it, but it should not be the primary concern. We stress that the selection of counterparties is of paramount importance as well as the simplicity of the structure and its market risk profile.

Amundi thinks that haircuts are the key to authorize a large list of securities as eligible without lowering the overall solidity of a transaction. A security of lesser liquidity or lower credit risk can only be eligible (i) under the condition of appropriate haircut (otherwise there would be a risk of excessive concentration on a few issuers) and (ii) provided that it reaches a minimum level of both credit quality and liquidity. In that respect we consider that the proposed minimum haircuts could well be insufficient in some instances and we express higher haircuts in our own policy.

Amundi sees a strong convergence between the rules expressed in the document for mitigating risk associated with cash collateral reinvestment and the effective limitations of exposure to risk expressed in the prospectus of money market funds and short term bond funds. We think that it should be clearly stated that investment in a fund that pledges to meet the proposed requirement in its investment strategy is eligible. We do see a major improvement and facility in operational terms if asset managers can offer funds that are eligible for reinvestment of cash collateral. At first sight, CNAV money market funds could not meet the criteria since their valuation might be slightly different from the market price, throwing a doubt on the fairness of the valuation.

6. Stress tests and disclosure:

Fund managers conduct regular stress tests on the liquidity risk of their portfolios. Liquidity management has always been considered as part of the service provided to investors together with the optimization of the risk /return of the portfolio. Redemption is a characteristic of Collective Investment Schemes. We do not think that stress tests results should be accessible to the public. We encourage authorities to require stress testing of collateral's disposability.

In terms of disclosure, funds will soon be required in Europe under SFT regulation to publish extensive reports. We believe that excessive information brings confusion more than it helps understanding and making good decisions. If a counterparty as participant to a contract owes detailed information to its co contractor, we do not think that disclosure should be extended to the public or competitors.

Thus, we support BCBS's approach about disclosure requirements between counterparties only. We suggest that UCITS and funds that pledge in their prospectus not to re-use be exempted to perform such a disclosure.

7. Methodology:

Amundi does not feel entitled to comment the methodology proposed to test that the minimum haircut level is reached both at the transaction level and the portfolio level. However, our understanding of a minimum is that the criterion is satisfied as soon as the effective value reaches the threshold. We consider that the equality between H and f should be acceptable.

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