Japan Securities Dealers Association
JSDA

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Secretariat of the Financial Stability Board
c/o Bank for International Settlements
CH-4002, Basel, Switzerland

RE: Comments to Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities

Dear Sir/Madam:

The Japan Securities Dealers Association (JSDA)[1] appreciates the opportunity to submit comments and responses on the consultative questions in the Financial Stability Board (FSB)'s "Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities" published on June 22, 2016.

1. General Comments

JSDA understands the background of this deliberation on the structural vulnerabilities of asset management activities and the importance of ensuring financial stability to prevent financial crises at the global level. We appreciate that the proposed policy includes various considerations to alleviate the risks in financial and capital markets. However, we are concerned about some proposed recommendations, since there appears to be room for further consideration of the rationale and consistency among their purposes and measures as well as cost-benefit comparison. Accordingly, JSDA hopes that the related parties will examine the following items in more detail in future discussions.

2. Comments on the Consultative Questions

(1) Measures for liquidity profile (Recommendation 1)

[1] JSDA is a self-regulatory organization (SRO) as well as an interlocutor for the securities industry. Its legal status is a Financial Instruments Firms Association authorized by the Prime Minister pursuant to Article 67-2, Paragraph 2 of the Financial Instruments and Exchange Act (FIEA). JSDA comprises around 500 members consisting of securities firms and other financial institutions operating securities businesses in Japan.

Although an asset may have sufficient liquidity at some point, the liquidity may vary with changes in the economic and market environment. The measures for liquidity profiling in terms of information gathering and classifying procedures should not be excessively complicated and should be feasible for asset managers as well as investors.

It is essential to establish simple measures as much as possible for liquidity profiling. Sufficient verification would be needed if an approach such as HQLA of LCR and RSF of NSFR in Basel III would be considered to achieve the purpose of the policy. The metrics to measure liquidity should be verified from multiple perspectives taking into account a broad range of market participants' opinions.

(2) Disclosure of liquidity profile (Recommendation 2)

Regarding disclosure of the liquidity profile, since liquidity can vary on a daily basis as mentioned above, evaluations and data about the profile can spread like wildfire and could mislead investors. Disclosure of the liquidity profile should be carefully deliberated, including its pros and cons.

At the time of a financial crisis, there is a risk that disclosure of decreasing liquidity may unintendedly alert investors and spur them to seek further redemptions. First, it is important to verify whether disclosure will perform its expected function of securing financial stability, and to confirm its effectiveness.

(3) Tools to manage liquidity (Recommendations 4, 5)

It is necessary to verify thoroughly whether imposing liquidity management at the level of each fund is the optimal approach to contributing to financial stability. A liquidity management tool constrains the investors' rights for redemption and should be positioned as a tool for use in exceptional circumstances.

Especially regarding "swing pricing", taking into consideration past cases, in some cases a NAV swings (declines) more than expected by investors and practitioners have found it difficult to enable investors to understand such cases. On the other hand, it is not clear to what extent the swing pricing system, where investors cannot know the range of the "swing" beforehand, can suppress the first-mover advantage.

The right to choose or combine tools, not only swing pricing but also other tools including partial redemption charges and deferred sales charges, should be reserved for the regulator of each jurisdiction in response to the unique circumstances and attributes of each jurisdiction.

(4) Implementation of stress tests (Recommendation 6, 9)

As a risk based approach, investment funds other than very large funds which have a significant impact on financial stability should be excluded from the scope of stress tests.
In Japan, information regarding purchases, redemptions, etc. of investment funds by investors is dispersively held by the distributing financial institutions. Implementation of stress tests at the level of each fund as well as at the system-wide level would impose a substantial burden on financial institutions. Accordingly, first it is essential to thoroughly examine what kind of test is effective to accomplish the purpose of the policy.

3. Conclusion

The consultative document states that some of these FSB policy measures are going to be embodied by IOSCO or related working groups at FSB from 2017. We hope that the policy measures are not treated as decided outcomes and that sufficient examination will be conducted considering the situation and characteristics of each region or jurisdiction.

Best regards

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