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IOSCO

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AFG comments on the IOSCO's consultation paper on CIS Liquidity Risk Management Recommendations

AFG's highlights

The Association Française de la Gestion financière (AFG)[1] welcomes the occasion given to comment on the IOSCO's consultation on CIS Liquidity Risk Management Recommendations. IOSCO has rightly tackled these liquidity issues as reducing systemic risk is among its three official objectives.

Our members are highly concerned by liquidity risk management. Liquidity risk management is an integral part of risk management and should be viewed and understood within this wider context.

IOSCO papers mention different regulatory works on this matter. It should be added that the asset management industry too had led works in the matter and issued guidance. Indeed, AFG has already issued several papers that are of interest to liquidity risk management issues:

- AFG Liquidity risk management tools in open-ended funds – May 2017

http://www.afg.asso.fr/wp-content/uploads/2017/05/2017_05_Liquidity_risk_management_tools_open-ended_funds-1.pdf

[1] The Association Française de la Gestion financière (AFG) represents the France-based investment management industry, both for collective and discretionary individual portfolio managements. 600 management companies are based in France. AFG members manage 3,000 billion euros, making the Paris fund industry a leader in Europe for the financial management of collective investments (with 1,500 billion euros managed from France, i.e. 19% of all EU assets managed in the form of investment funds). In the field of collective investment, our industry includes – beside UCITS – the whole range of AIFs, such as: employee savings schemes, regulated hedge funds/funds of hedge funds, private equity funds, real estate funds and socially responsible investment funds. AFG is an active member of the European Fund and Asset Management Association (EFAMA) and of PensionsEurope. AFG is also an active member of the International Investment Funds Association (IIFA).

- AFG Code of Practice on liquidity risk management in Collective Investment Schemes (CIS) – January 2016

http://www.afg.asso.fr/wp-content/uploads/2016/02/Guide%20Professionnel_Liquidite_2016_ENG.pdf

- (already mentioned by IOSCO) AFG Code of conduct for asset managers using Swing Pricing and variable anti-dilution levies (ADL) - 2014 / Modified January 2016

http://www.afg.asso.fr/wp-content/uploads/2014/06/GuidePro_SwingPricing_actualise_2016_ENG.pdf

We believe the 2013 IOSCO's Liquidity Report contains already the key messages for the subject of liquidity risk management. Limited refinements will permit to ensure the Liquidity Report addresses the FSB recommendations following the work on the structural vulnerabilities in asset management. In our view, the financial stability focus shall allow the principle of proportionality for liquidity risk management. We agree that this focus should be viewed in conjunction with investor protection considerations as the asset management is an individually fund segregated sector that follows an agency model.

One crucial element that IOSCO mentions is the fact that the aim of fair treatment of investors is consubstantial to an effective liquidity risk management. Clearly stating this overarching principle helps to apply subsequently the adapted set of measures regarding liquidity risk management. We appreciate the in depth and useful work done by IOSCO in the "Good practices document" and insist on this document being understood as a reference point and not as a recommendation or requirement. Every fund is different and it can evolve in an infinite type of market liquidity contexts. Flexibility is therefore key.

We would also like to recall that liquidity is not a stable concept and there should be flexibility in the manner firms handle with the matter so as to be efficient relative to the market stance. AFG considers that it is not possible to know with certainty what impact future events might have on portfolio holdings and that over (ante) reacting may also prove to be harmful by advancing or exacerbating a market situation.

We agree with IOSCO regarding the highly relevant link between liquidity and valuation.

AFG insists on the distinction to be made between redemptions and runs. Funds may encounter situations of high redemptions and be perfectly able to deal with them (IOSCO cites by the way some examples). Runs are very particular events, highly rare and extreme in nature. They are linked to an "embedded" first mover advantage, like it was the case with the implicit guarantee on CNAV funds sold in the US. AFG disagrees with IOSCO regularly mentioning in these two consultation papers of the "first mover advantage" associated with funds in general.

Regarding stress tests, it should be reminded that they are not a management tool. They may give useful information that is brought to knowledge to the manager who has at his disposal an extensive set of elements to take into account when making investment decisions. Stress tests represent a check tool which should not be set so as to trigger investment decisions. If not, this tool risks to generate herding behaviours that ultimately may bring systemic risk.

Last but not least, even if we totally agree to the importance of the liquidity risk management as a general rule, we would like to caution against a certain "dictatorship" of liquidity. Indeed, the tendency to privilege liquidity over longer term assets and investment vehicles impedes more stable financing of the economy. In addition, disclosures on the liquidity risks should not isolate and overemphasize this

risk in particular compared with the general risk and return profile of the fund. In a recent document concerning sustainable finance, the European Commission stated that the goal was "a financial system that promote sustainable economic development rather than boom and bust". Envisaging that there is merit in setting up immediate liquidity "buckets" in all types of funds is a false good idea. This cushion represents one technique that may be adapted in some situations, such as for instance for funds where the expectation in terms of liquidity is high as this is identified as the promise of the fund to its investors (money market funds for instance).

Please see hereafter AFG's remarks to IOSCO's specific questions:

Q1. The 2013 Liquidity Report related to open-ended CIS and, where determined by the responsible entity, to some closed-ended CIS. Should the proposed text laid out below apply also to the same range of CIS? Should certain CIS or types of CISs be excluded from any particular requirements, or be subject to a different requirement, because of their investment strategies, ownership concentrations, redemption policies, or some other factor that makes them more or less prone to liquidity risk?

Yes. Regarding the scope of application of the Recommendations, AFG totally agrees with IOSCO in keeping the same scope as for the 2013 Recommendations, i.e. open-ended CIS and, where determined by the responsible entity, some closed-ended CIS. Mandates are excluded from the scope.

We believe that funds are very different regarding the liquidity subject, ie they may have very different tolerance (or sensitivity) to the liquidity risk. Thus, investment funds do not all necessitate the same liquidity tools and not at the same time/stage of market stress. Nevertheless, access to liquidity tools should be universal so as when needed, solutions are available.

AFG has issued two papers regarding the liquidity issue where liquidity risk management principles are detailed (AFG Code of Practice on liquidity risk management in Collective Investment Schemes (CIS) – January 2016) and where different tools available are described on an illustrative scale (AFG Liquidity risk management tools in open-ended funds – May 2017).

Q2. Do respondents agree with the general considerations around liquidity risk management? Are there other issues that should be included?

Yes, AFG agrees with the general considerations around liquidity risk management. We do not see other issues to be included apart a clear mention of flexibility and proportionality in the approach.

We believe the 2013 IOSCO's Liquidity Report contains already the key messages for the subject of liquidity risk management. Limited refinements will permit to ensure the Liquidity Report addresses the FSB recommendations following the work on the structural vulnerabilities in asset management. In our view, the financial stability focus shall allow the principle of proportionality for liquidity risk management. We agree that this focus should be viewed in conjunction with investor protection considerations as the asset management is an individually fund segregated sector that follows an agency model.

One crucial element that IOSCO mentions is the fact that the aim of fair treatment of investors is consubstantial to an effective liquidity risk management. Clearly stating this overarching principle helps

to apply subsequently the adapted set of measures regarding liquidity risk management. We appreciate the in depth and useful work done by IOSCO in the "Good practices document" and insist on this document being understood as a reference point and not as a recommendation or requirement. Every fund is different and it can evolve in an infinite type of market liquidity contexts. Flexibility is therefore key.

We would also like to recall that liquidity is not a stable concept and there should be flexibility in the manner firms handle with the matter so as to be efficient relative to the market stance. AFG considers that it is not possible to know with certainty what impact future events might have on portfolio holdings and that over (ante) reacting may also prove to be harmful by advancing or exacerbating a market situation.

We agree with IOSCO regarding the highly relevant link between liquidity and valuation.

Q3. Does the Good Practices Document cover the key considerations regarding liquidity risk management tools, including their use in normal and stressed scenarios? Are there other issues that should be considered? Are there other key tools that should be included? Do you agree with the pros and cons in regards to the use of each tool? Are there other pros and cons that should be considered?

Yes, AFG thinks that the Good Practices Document generally covers the key considerations regarding liquidity risk management tools, including their use in normal and stressed scenarios. We would recall that AFG has also issued an educational paper on the different tools available for French open ended vehicles (AFG Liquidity risk management tools in open-ended funds – May 2017).

AFG would like to insist on the fact that these represent examples of good practices and that they should not give rise to guidelines or recommendations.

Q4. Do you agree with the general considerations regarding stress testing? Are there other issues that should be included?

Yes, we agree with the general considerations regarding stress testing.

It should be clearly reminded that stress tests are not a management tool. They may give useful information that is brought to knowledge to the manager who has at his disposal an extensive set of elements to take into account when making investment decisions. Stress tests represent a check tool which should not be set so as to trigger investment decisions. If not, this tool risks to generate herding behaviours that ultimately may bring systemic risk.

Q5. Should ETFs be subject to different liquidity requirements than other CIS? a) If not, should ETFs be included within the scope of the 2017 Liquidity Recommendations?

(i) If yes, are changes needed to be brought to the 2017 Liquidity Recommendations to reflect ETFs specificities? Which ones?

(ii) If not, please explain why ETFs should not be included within the scope of the 2017 Liquidity Recommendations if they have partly similar liquidity issues as other CIS.

b) If ETFs should be subject to different liquidity requirements than other CIS, what should they be?

First, we would like to remind that ETFs are framed as UCITS funds in Europe. They already comply with UCITS rules and expectations. Key elements of the framework include: a fiduciary duty for the management company to act in the best interest of the fund and of investors; that the assets of the fund are held separately from the management company's balance sheet; that there is an independent depositary that oversees the activity of the manager and safeguards the assets; and that the manager is subject to detailed requirements relating to the management of conflicts of interest; there are limitations and rules for the calculation of the global exposure.

ETFs are UCITS index funds. As index funds, they behave as any other fund and are subjected to the same rules. In addition to these features, ETFs have some other specific features related to secondary dealing market.

In our members' view, ultimately, the liquidity of the ETF is mainly defined by the liquidity of the underlying market and they do not engage to offer liquidity in all market conditions. Thus, regarding the liquidity risk for ETFs, their liquidity is correlated to their underlying index. Indeed, an ETF is liquid if its underlying index is liquid. The nature of the underlying index is the determining factor of the effective liquidity of an ETF. If an underlying market was less liquid, the ETF market maker would widen the quotations' spreads intra-day to take into account the difficulties he encounters to cover in the underlying market.

We continue to believe that is not appropriate to look specifically to ETFs, to the extent that they are only CIS and that they are not different (in Europe). ETFs are users of most of the liquidity tools available for open ended funds (such as swing pricing, anti-dilution levies, in kind redemptions, subscription temporary closes, redemption suspensions, etc.). There are however specific aspects with ETFs, for example market making and everything that relates to the secondary market.

In that respect, ETFs (unlike the other UCITS funds) must also abide by a second set of rules, which are the "listing rules" such as the obligation to publish an indicative NAV, to publish an intra-day NAV that observes the spread limits and minimal bid/ask spreads, to have several market makers etc. European ETFs are regulated by two set of rules concomitantly.

In addition, ESMA issued guidance in 2012 on ETFs and other UCITS issues. These guidelines address (among other subjects) some secondary market issues for ETFs, in particular contingency planning. The ESMA guidelines require that in certain circumstances, investors who acquire their units or shares on the secondary market be allowed to sell them directly back to the ETF.**Q6. Are there key liquidity related issues specifically regarding ETFs?**

As mentioned earlier at Q5, the only specificity lies with the secondary market aspects. However, these aspects, should not give rise to a perception of a liquidity different from that of the underlying market/index. Disclosures are useful so as the investor be aware of these secondary market aspects.

Q7. Does this guidance on the design phase process capture the best of current good practices in the design of CIS?

Yes, we believe that it generally does. Please see however some remarks hereafter:

o Recommendation 3:

We suggest to delete the italic sentence starting with *"Often responsible entities…less liquid."*, because this comment does not represent a "Guidance".

o Recommendation 4:

In the Guidance, we suggest to delete the word "*documented*". While Recommendation 4 itself is only asking for "appropriate" arrangements, the proposed Guidance is further narrowing down the meaning of this Recommendation. The request for "documentation" is not always appropriate and may in many cases represent a heavy unnecessary burden.

Regarding the proposed Guidance on p. 10, second §, we suggest to:

- Add "*where appropriate*" after "*should be subject*"

- Put a full stop after "*responsible entity*", in order to avoid the submission of all reviews and updated to the Board. It would read: *"(...) responsible entity.* ***The fund liquidity risk can be thereafter monitored on an ongoing basis and therefore the set-up of monitoring tools can be reviewed and updated by both portfolio management and risk management teams****."*

Regarding the "Liquidity Risk Management Practices – Liabilities" section, we think there are good ideas, but this section should remain a principle and not go too far. First, some investment funds may be used as component bricks to a smorgasbord of different strategies or types of investors. There could be some serious drawbacks regarding the definition of too strict target categories. In addition, it is general knowledge that we don't know all our investors that may invest through different channels. This section should be more cautious and use a mention that this guidance works only "*if meaningful*" or "*if relevant*". To be exact, this section should have preferably asked that due regard is paid to the risk/reward profile of the fund and to its unambiguous disclosure to investors. The ultimate objective is for investors to understand / comprehend the promise of the fund and how it is supposed to behave in simple market contexts. Broad target categories make sense (retail, institutional...), but it is the ultimate decision of the investor to accept or not the specific risk/reward inside a broad category.

Regarding the "Liquidity Risk Management Practices – Assets" section, we agree with IOSCO that not all suggestions are applicable in all situations. We would like to recall that in Europe, UCITS fund invest in assets which are considered liquid by nature. The frontier of the actual more or less liquidity in the market may fluctuate and we prefer in Europe to speak in terms of eligible or non-eligible assets. Setting an arbitrary limit when investing on a certain market related definition of "illiquid" assets is an uneasy concept. Regarding the "*limits on time allowed to correct unintended limit breaches*", we prefer the UCITS concept which does not define any timeframe, but subjects it to the manager acting in the best interest of unitholders.

Q8. Does Recommendation 7 capture appropriate additional liquidity disclosures?

No, we generally do not agree with what is proposed. AFG believes that liquidity risk management details must remain non-public, but made available to regulators. Some confidentiality should be kept so as not to undermine the efficiency of the risk measure. For instance, AFG backed by AMF has issued Guidance regarding the swing pricing mechanism where the manager is encouraged to give "*only general principles of the chosen methodology. Furthermore, it should not disclose parameters that are too detailed and recent so that to enable an investor to amend his/her subscription or redemption strategy so as to take advantage of more advantageous conditions and thus reduce the Swing Pricing mechanism's efficiency. In particular, the management company does not communicate (in writing or orally) the current levels of the trigger thresholds. To this end, it notably ensures that the internal circuits of information are restricted to favour the conservation of the confidential character of this piece of information.*"

- Recommendation 7:

We suggest deleting the following two §:

A commitment in the initial offering documentation to provide to investors on a periodic basis and where appropriate, on an aggregate basis, information regarding the investment portfolios of the CIS that may allow investors to assess the liquidity risk attached to the CIS e.g. holdings of various asset classes/types of securities, detailed holdings of individual securities;

Disclosure in the CIS offering documents of the general approach the CIS will take in dealing with situations where it is under liquidity pressure from a heightened level of net redemption requests.

We do not believe that recommending such a commitment may provide to be useful in all cases. All investors do not have the same knowledge that permits to assess the liquidity attached with holdings. Also, the asset side is to be linked with the liability side to have a meaningful view, which is the manager's job. Ultimately, the investor buys a CIS that is managed by a professional, not a collection of holdings.

We would delete the second bullet for a reason of confidentiality vis-à-vis the market – mentioned by IOSCO itself later in the text – it would be dangerous to disclose such an approach. Conversely, we agree on saying for instance: *"The CIS will have to set contingency plans covering the situations (...). Such contingency plans will remain at the disposal of the regulator."*

Regarding the next two §, they should be replaced by a simple and meaningful Guidance: "*The liquidity management process and the liquidity management tools that may be employed by the CIS should be appropriately disclosed in the CIS's* ***prospectus****. Sufficient detail should be disclosed to make investors aware of material liquidity risks."* Delete all the rest. Describing the relevant tools that are available is appropriate and sufficient. For a confidentiality reason and efficiency of the fund's risk management, it would be dangerous to disclose more in detail.

Q9. Should additional wording be included in Recommendation 12 concerning how responsible entities should proceed when faced with the need to sell assets to the extent that might lead the CIS to vary from its investment strategy?

No, these are situations where the skill of the asset manager and the type of market situation cannot be anticipated with accuracy through a Guidance.

We suggest that the Recommendation 12 wording be refined as follows:

Recommendation 12

The liquidity risk management process should ***seek to*** *facilitate the ability of the responsible entity to identify an emerging liquidity shortage before it occurs.*

Q10. Does the proposed additional guidance under Recommendation 13 constitute the appropriate approach for a CIS to assess its redemption obligations and liabilities? If not, what else would you suggest?

o Recommendation 13:

We believe this recommendation is appropriate, as knowing one's investors is a significant plus. However, this recommendation should acknowledge two important points:

1. The actual stage of knowledge, access to information and process to identify patterns and profiles is still at a very early stage. We need to have the time to gain in maturity and also for the ecosystem to accept to give us this information on end clients and not invoke confidentiality reasons. Also, a multiple listed fund would have difficulty to gather information in the same time in all markets so as to be able to aggregate knowledge on the liability side in a meaningful way and that coincides with the portfolio analysis's timeframe. This is why the wording "could" should be used and as long with the conditional mode as frequent as possible. This should be clearly understood as an "objective of means", not of result. Also, this way of drafting reinforces the principle of proportionality.

2. One should not make too much emphasis on the usefulness and achievements on the liability analysis. This is not an exact science and when a serious crisis arises, no profiling or other means employed might prove helpful. We have also to insist on the fact that "getting the big picture" on the major holdings by clients will certainly be effective and there is no need to go identify each retail holding so as to aggregate it to finally know that the "Carpentras widow" holds 0,05% or 0,07% of the fund. Cost efficiency is key so as to be able to have the big picture early enough…

"This investor base knowledge could include investor profiles of the various types of investors which may allow the responsible entity to understand why investors are investing in the CIS, their risk appetite and in what circumstances they may wish to redeem. The responsible entity ***could*** *conduct assessments of the characteristics of the investor base in a CIS, analyse the potential impact that these characteristics have on the level of redemptions under different scenarios and take this into account in liquidity management for the CIS.*

Data on liabilities such as collateral needs and potential margin calls, ***could*** *be assessed alongside potential redemption demands."*

Our members also propose to redraft the sentence underlined. It would read: "Where possible, ***the relevant intermediaries should interact with responsible entities to secure compulsory pre-notification in reasonable time before removal (…)"***: it is key to oblige intermediaries to inform fund managers in due time, in order to anticipate in the best conditions the removal from the best-buy list and thus management the potential consequences on the fund management in the best way – to the benefit of both investors and the market.

In conclusion, it is highly relevant to be aware that even if knowing one's investors may be a significant plus, the practical means to achieve this as well as setting the meaningful level of detail are very problematic today. We thus recommend that discussions around liability side knowledge be principle based.

Q11. Are there procedures or practices that responsible entities currently use to implement their stress tests which have been found to be particularly informative to responsible entities and which are not consistent with or included in the approach set out here? If so, please provide examples.

No.

Q12. Are there procedures or practices that responsible entities have not found to be particularly useful which the proposed approach to liquidity stress testing would encourage and why?

Yes. IOSCO mentioned credit rating downgrades. In theory, this could be seen as a meaningful suggestion, but in practice, it may be counterproductive. Indeed, what IOSCO proposes, some regulators may want to apply and in that respect, the latter may ask managers to pay all CRAs so as to be sure all data is powered into the stress test tool. Such an idea will have dramatic consequences in terms of fees and ineffective measure for asset managers and ultimately will lead to systemic risk. We had the experience with MMFs, and once a regulator mentions CRAs, there is difficulty to end with an operationally meaningful practice. Our managers have already downgrades in mind (if meaningful), there is no need for IOSCO or subsequent regulation to name it (for evident reasons explained before). We suggest to delete the example in the 4th § on page 15 related to credit rating downgrades as well as the phrase related to stressing the "reputational" risk. This is going too far; if there is a specific need related to a "reputational risk" of an entity or a sector, this is very particular and does not need to be mentioned here.

Regarding stress tests in general, it should be reminded that **they are not a management tool**. They may give useful information that is brought to knowledge to the manager who has at his disposal an extensive set of elements to take into account when making investment decisions. Stress tests represent a check tool which should not be set so as to trigger investment decisions. If not, this tool risks to generate herding behaviours that ultimately may bring systemic risk. IOSCO should therefore not leave the impression that stress tests have a direct link with portfolio management, so we propose some redrafting:

*"Stress testing results **may** have the potential to contribute, as appropriate, into all stages of the CIS's product life cycle, including in the product design stage when determining the dealing and distribution arrangements ~~and asset composition~~, and in performing investment and liquidity risk management (~~e.g. in calibrating holdings of liquid assets and other investments~~, and the use of different liquidity risk management tools and contingency planning) on an ongoing basis."*

We disagree with obligations to have forward looking scenarios. This kind of scenarios are very specific and rare, IOSCO should reformulate so as to avoid inappropriate guidance:

*Appropriate stress testing should be carried out based on normal and stressed scenarios (for example, atypical redemption requests). Scenarios **could** include backward-looking historical scenarios and/**or if relevant** forward looking hypothetical scenarios, and could be based on parameters calculated using statistical techniques or concrete stress events.*

Last, but not least, stress tests should not be given an exaggerated importance; they are a risk management tool among others. Also, please pay attention to any commercially driven interests in the stress testing matters. Indeed, stress testing risks (because of heightened regulatory interest) to become a high cost for asset managers with little added value compared to other tools they already use.

Q13. Is the proposed approach to the design and operation of stress testing processes realistic and does it deal with the key issues?

Generally yes, but for the remarks already expressed at Q 12.

Q14. Does the proposed additional guidance under Recommendations 3, 7 and 12 add effectively to the available guidance?

Generally yes, but for the remarks we have suggested at previous questions.

Q15. Does Recommendation 14 capture the best of current good practices in stress testing?

Generally yes, but for the remarks already expressed at Q 12. Proportionality and conditional formulations are key so as not impose inappropriate or ineffective requirements of funds and management styles that are all different.

Q16. Does the recommendation add up to an effective testing procedure which will lead to the smooth triggering of applicable liquidity management tools when appropriate?

Yes. These seem to be sensible and reasonable steps, but each firm should be able to implement its own process.

Q17. Other than those examples listed above, are there any additional scope and/or aspect that you consider necessary and appropriate to be included as part of the contingency plan for an effective implementation of liquidity management tools by CIS/responsible entities?

It should be clear however that contingency plans are secondary in nature and are not supposed to be often triggered. Thus, there should be some persistency recognised and no obligation to update and stress a contingency plan too often. Otherwise, it would be costly and meaningless.

Q18. How do existing CIS envision transitioning to Recommendation 17?

AFG has initiated with AMF a certain number of works so as to develop the French regulatory context with regards to liquidity tools available. Gates were introduced in the French Law in 2016 and as of March 2017, the AMF set of rules completed the regulatory guidance/requirements. Currently discussions are engaged so as to be able to complete the French regulatory set with tools such as in kind redemptions, simple notice periods and soft/hard closes.

It should be mentioned that asset managers do not trigger exceptional liquidity tools with light-heartedness as there is some reputational risk attached to such situations. Often, there is a "first mover disadvantage" to trigger a tool. Therefore, it should be clear that these tools are not meant to be used for the asset managers' convenience. These tools are meant to protect investors and fair treatment.

AFG specific comments on the IOSCO "Good Practices" document

- First, such a document should be available in all IOSCO members' languages because actors need to be able to understand it and refer to it if they need so. It is therefore frustrating that native English speaking companies and global companies be advantaged in this IOSCO process.

- Second, AFG thinks this paper is well written with useful examples of good practices and that it gives interesting views on different countries' practices.

More specifically, please see our remarks:

- We appreciate the in depth and useful work done by IOSCO in the "Good practices document" but insist on this document being understood as a reference point and not as a recommendation or requirement. Every fund is different and it can evolve in an infinite type of market liquidity contexts. Flexibility is therefore key. We would also like to recall that liquidity is not a stable concept and there should be flexibility in the manner firms handle with the matter so as to be efficient relative to the market stance. AFG considers that it is not possible to know with certainty what impact future events might have on portfolio holdings and that over (ante) reacting may also prove to be harmful by advancing or exacerbating a market situation.

- If we agree that some transformation is consubstantial in a collective scheme, we do not think that it is of magnitude. On the contrary, excess transformation bears too high risks and this subject has already been analysed by the FSB within systemic risk discussions. Therefore, we continue to advocate that there is no transformation risk with mutual funds.

- Our members are highly concerned by liquidity risk management. Liquidity risk management is an integral part of risk management and should be viewed and understood within this wider context.

- Regarding the continuous monitoring of liquidity, AFG totally disagrees with the bucketing method and with the idea of maintaining "sterilised" liquidity in all funds. Envisaging that there is merit in setting up immediate liquidity "buckets" in all types of funds is a false good idea. This cushion represents one technique that may be adapted in some situations, such as for instance for funds where the expectation in terms of liquidity is high as this is identified as the promise of the fund to its investors (money market funds for instance). Sterilising all that money globally is also totally counterproductive in terms of investment for the financing of the economy. We propose to avoid any confusion and delete the second bullet point on the middle of page 5.

- Regarding the definition of "liquid assets", we would like to recall that in Europe UCITS fund invest in assets which are considered liquid by nature. The frontier of the actual more or less liquidity in the market may fluctuate and we prefer in Europe to speak in terms of eligible or non-eligible assets. Setting an arbitrary limit when investing on a certain market related definition of "illiquid" assets is an uneasy concept. Regarding the "limits on time allowed to correct unintended limit breaches", we prefer the UCITS concept which does not define any timeframe, but subjects it to the manager acting in the best interest of unitholders. We suggest to delete the two parenthesis on the last two bullet points on top pf page 8.

- AFG would like to recall that knowledge on the investors base is still at work, at a very early stage. We need to have the time to gain in maturity and also for the ecosystem to accept to give us this information on end clients and not invoke confidentiality reasons. One should not make too much emphasis on the usefulness and achievements on the liability analysis. This is not an exact science and when a serious crisis arises, no profiling or other means employed might prove helpful. We have also to insist on the fact that "getting the big picture" on the major holdings by clients will certainly be effective and there is no need to go identify and aggregate each retail holding. Cost efficiency is key so as to be able to have the big picture early enough…

- This being said, in order to provide sustainable finance to sustainable economic growth, there is a need to match long term savings with long term investment. In such a context, liquidity should not be the unavoidable requirement for any type of fund. It is a requirement for UCITs but the market needs long term AIFs shaped for retail investors that could invest in long term assets. For

these funds, liquidity requirements should be very different and this would be to the benefit of investors who could get better returns and be less exposed to short term fluctuations of markets.

- We agree with IOSCO regarding the highly relevant link between liquidity and valuation.

- AFG insists on the distinction to be made between redemptions and runs. Funds may encounter situations of high redemptions and be perfectly able to deal with them (IOSCO cites by the way some examples). Runs are very particular events, highly rare and extreme in nature. They are linked to an "embedded" first mover advantage, like it was the case with the implicit guarantee on CNAV funds sold in the US. AFG disagrees with IOSCO regularly mentioning in these two consultation papers of the "first mover advantage" associated with funds in general.

- Regarding gates, we agree with IOSCO that they may be used in certain normal conditions for certain types of funds. It may be added as an *Advantage* in the table for Gates that it is a step before suspension, it may help in intermediary situation instead of using the last recourse arm which is the suspension.

- AFG believes that liquidity risk management details must remain non-public, but made available to regulators. Some confidentiality should be kept so as not to undermine the efficiency of the risk measure. For instance, AFG backed by AMF has issued Guidance regarding the swing pricing mechanism where the manager is encouraged to give "*only general principles of the chosen methodology. Furthermore, it should not disclose parameters that are too detailed and recent so that to enable an investor to amend his/her subscription or redemption strategy so as to take advantage of more advantageous conditions and thus reduce the Swing Pricing mechanism's efficiency. In particular, the management company does not communicate (in writing or orally) the current levels of the trigger thresholds. To this end, it notably ensures that the internal circuits of information are restricted to favour the conservation of the confidential character of this piece of information.*"

- Regarding the Side Pockets, AFG would like that be added as an *Advantage* in the table that the Side Pocket ensures fair treatment among investors as they get an equal share on the illiquid/distressed portion of the portfolio. We do not agree that Side Pockets be mandatorily mentioned in the Prospectus in order to be allowed to use them. It is preferable in an extreme case such as a fraud to be able to segregate the distressed part than to suspend / liquidate the entire fund.

- Regarding the notice period, we only partially agree with the disadvantage related to the perception of investors. It is not the same thing to be able to invest/get out only on Mondays than to be able to do it every day, but think to notice it to the fund manager one week before. Once explained, investors can understand very well the difference. It should be clearly mentioned that the notice has a fixed term so as to give certainty to the investor on the date of the flows, but this does not mean that the manager will systematically use the notice period.

- Regarding the in kind redemption table, some advantages disadvantages are unclear and we would remark that the argument saying the *"equal treatment of investors comes into question as there will always be some losers"* is not specific to in kind redemptions…

- Regarding stress tests, it should be reminded that they **are not a management tool**. They may give useful information that is brought to knowledge to the manager who has at his disposal an

extensive set of elements to take into account when making investment decisions. Stress tests represent a check tool which should not be set so as to trigger investment decisions. If not, this tool risks to generate herding behaviours that ultimately may bring systemic risk. We disagree when IOSCO says that stress tests can be used to "tailor the CIS's composition", to "inform investment decisions", etc. We agree that aggregated stress tests are a rare exception, for instance relevant only when the manager has several S/C funds that taken together make a highly significant proportion of the free float. Fund stress tests guidance should be kept at individual level. There should be no mandatory design of scenarios. Collateral stress testing should be envisaged only when it is material in the fund strategy. AFG wonders what IOSCO means when citing the algorithmic trading as an event to be taken into account in stress tests. Regarding the "Use of stress testing section" **we would like to correct that AMF has not issued any "explicit requirements" on stress tests.** AMF's document on stress tests is a non-binding Guide, it is a collection of examples. AFG continues to totally disagree with any binding requirements in the matter; it would be counterproductive. In addition, the use of stress test results is like any other risk management tool, at the disposal of the fund management, but does not trigger any automatic investment decision.

- Last but not least, even if we totally agree to the importance of the liquidity risk management as a general rule, we would like to caution against a certain "dictatorship" of liquidity. Indeed, the tendency to privilege liquidity over longer term assets and investment vehicles impedes more stable financing of the economy. In addition, disclosures on the liquidity risks should not isolate and overemphasize this risk in particular compared with the general risk and return profile of the fund.

If you need any further information, please don't hesitate to contact me at +33.1.44.94.94.31 (a.gurau.audibert@afg.asso.fr).

Sincerely Yours,

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