Cross-border Derivatives Regulation

DRAFT

Better Markets' Summary Presentation

June 12, 2013

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Coming to a **U.S.** City Near You? The Cost of the CFTC Not Getting Cross Border Right

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Essential to Protect the American People, Financial System, Economy

- Derivatives market was where the last crisis
  - Was invisibly incubated
  - Ignited the financial crisis
  - Acted as a conveyor belt to transmit the crisis throughout the globe
  - Cost trillions of dollars of losses
- That's why the CFTC was given the **statutory mandate** to regulate cross border derivatives activities

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Costs to U.S. have been staggering

- Too much of financial reform discussion is antiseptic, academic, bloodless & historical
- Financial reform necessary because
  - **Worst** financial collapse since 1929
  - **Worst** economy since the Great Depression
  - Report: Going to **cost the U.S. $12.8+ trillion**
- Money, however, tells only part of the story of lives, families, communities suffering from coast to coast

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THE COST OF THE WALL STREET-CAUSED FINANCIAL COLLAPSE AND ONGOING ECONOMIC CRISIS IS MORE THAN $12.8 TRILLION

A Report From

BETTER MARKETS
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September 15, 2012

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That's not all even close to all the costs

- Doesn't include fiscal policy costs:
  - Much of annual $1 trillion deficits due to increased expenditures and decreased tax receipts from the financial & economic crises
    - Most of discussion about cuts due to those costs
- Doesn't include monetary policy costs:
- Unprecedented zero interest rate policy (ZIRP) AND
- Unprecedented asset purchases resulting in a $3+ trillion Fed balance sheet
- All necessitated by the financial collapse & economic crisis it caused

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SEC Proposed Rule is Inapplicable to CFTC

- The SEC was given statutory authority limited solely to anti-evasion and no mandate regarding cross border jurisdiction
- The CFTC was given the same anti-evasion authority, but also given an affirmative, expansive statutory mandate to regulate cross border derivatives activities

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SEC Statute:

"(c) Rule of construction. No provision of this title [15 USCS §§ 78a et seq,] that was added by the Wall Street Transparency and Accountability Act of 2010, or any rule or regulation thereunder, **shall apply** to any person insofar as such person transacts a business in security-based swaps **without the jurisdiction of the United States, unless** such person transacts such business in contravention of such rules and regulations as the Commission may prescribe as **necessary or appropriate to prevent the evasion of any provision of this title** [15 USCS §§ 78a et seq,] that was added by the Wall Street Transparency and Accountability Act of 2010…."

Section 772(b) of the DFA

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CFTC Statute:

"(i) Applicability. The provisions of this Act relating to swaps that were enacted by the Wall Street Transparency and Accountability Act of 2010 (including any rule prescribed or regulation promulgated under that Act), **shall not apply to activities outside the United States unless** those activities—

(1) have a direct and significant connection with activities in, or effect on, commerce of the United States; or

(2) contravene such rules or regulations as the Commission may prescribe or promulgate as are **necessary or appropriate to prevent the evasion of any provision of this Act** that was enacted by the Wall Street Transparency and Accountability Act of 2010."

Section 722(d) of the DFA

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Derivatives Market Jurisdiction: CFTC 96.5%, SEC 3.5%

- Of the immense derivatives markets, the SEC has jurisdiction for only the tiny securities based swaps portion of the markets
  - This is, at most, 3.5% of the derivatives market
- The CFTC has jurisdiction for 96.5% of the derivatives market
  - Plus, the CFTC has the expertise & decades of experience with derivatives

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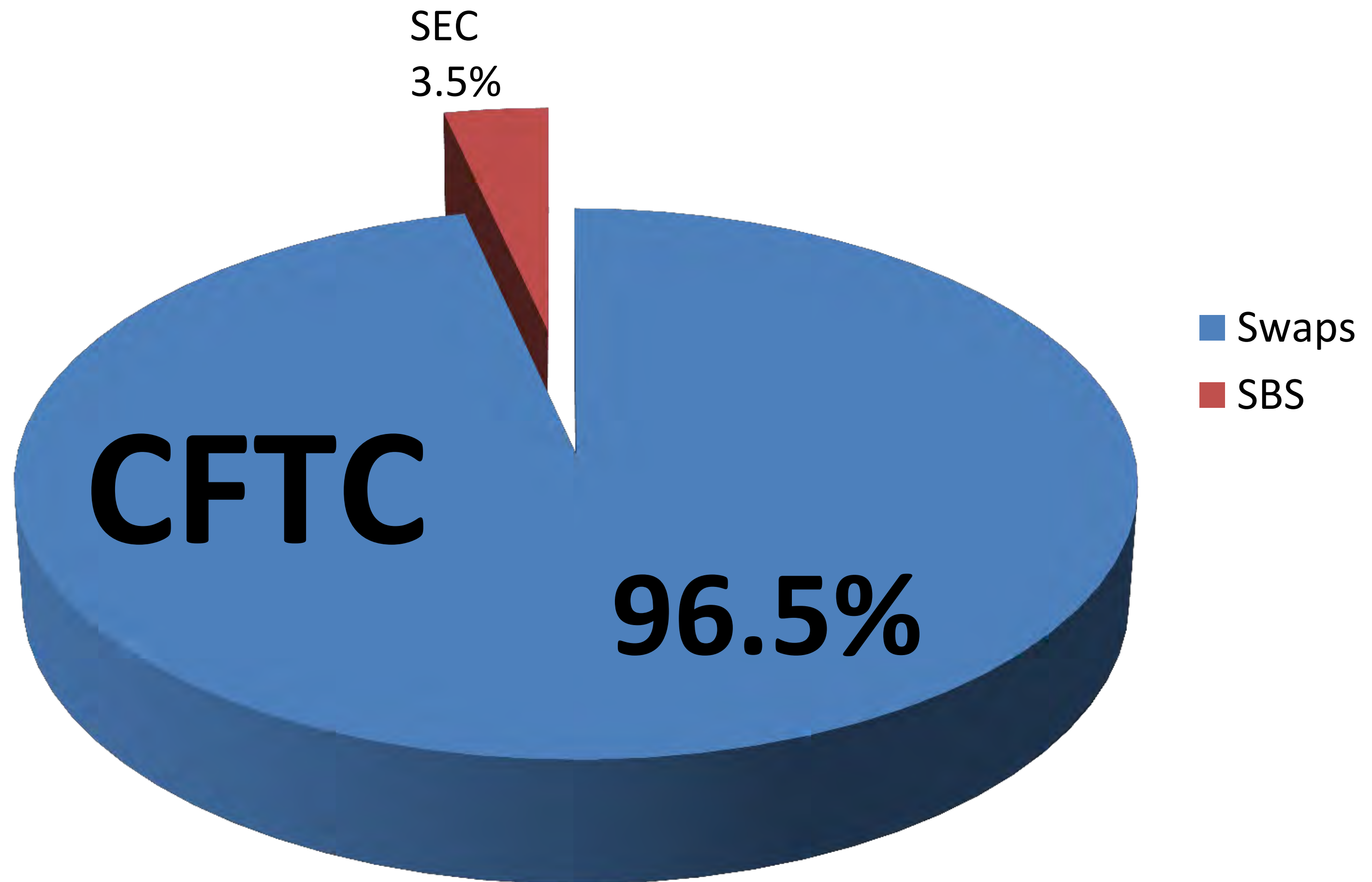
Relative Proportions of Swaps and Security Based Swaps



Source: BIS Annual derivatives market report, 2012. Note, if either DTCC data or CFTC-reported data were used, the SEC portion of the market would be under 3%. Thus, 3.5% is the maximum.

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Turning the World Upside Down

The CFTC following the SEC's views under these circumstances turns the world upside down

- It would be as if CFTC regulations were applied to 100% of mutual funds because less than 1% of mutual funds are also regulated by the CFTC as CPOs
  - Never happen
    - Shouldn't happen
    - With cross border or anything else

CFTC Should **Not** Wait for the SEC

- It would be irresponsible for CFTC to wait for the SEC
- SEC at very beginning of their regulatory process
  - Just proposed a rule on May 1, 2013
    - Not even any substantive comments yet
- CFTC has been working on cross border for
    - 2 ½ years, beginning before January 2011
    - Proposed guidance June 2012
      - » After 1 ½ years of deliberation, including huge industry input
    - After yet more consideration, further guidance in Dec. 2012
    - After even more input, latest draft circulated May 16, 2013
    - Deadline of July 12, 2013 set 7 months ago
    - Already too many delays

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SEC Proposed rule is weak & will be ineffective in achieving CFTC legal mandate

- The SEC proposal will almost certainly be the starting gun for a global race to the bottom
  - Talks a lot about focusing on risk, but the rule itself focuses on the form of entities, making arbitrage relatively easy
  - Recognizes risk from guaranteed affiliates, but then excludes them
  - Takes a territorial approach, but allows substituted compliance even within the territorial United States (as to external bus conduct standards)

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SEC Substituted Compliance is weak, nontransparent, fails to protect the U.S. & invites regulatory arbitrage

- SC not in DFA & of questionable legal basis
- SEC proposed rule focuses on so-called "holistic" approach to regulation and purportedly comparable "outcomes," but in only 4 overly broad categories
- SEC proposes to consider irrelevant factors not in the statute & which will put the U.S. at risk
- SEC proposes a process that lacks transparency & fails to ensure public notice or input

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Federal Reserve Bank rejecting failed substituted compliance

- Pre-crisis regulation in the U.S. of foreign bank subsidiaries and branches largely left to home country regulation
- Financial crisis revealed that to be total failure
- Now, Fed proposed rule on foreign bank organizations (FBOs) requires them to form an intermediate holding company subject to Fed regulations on capital, etc.

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Required harmonization already done

- Congress ensured that the scope did not go beyond U.S. interests by expressly limiting the scope of the law to only certain activities
  - Only duty to "consult & coordinate … **to the extent possible**," which has been done
- **Law clear: consult, not subordinate; then act** to reduce risk to U.S. from cross border activities as mandated by the law

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There are no conflicts with international regulators

- No conflicts b/c no one has passed comprehensive Title VII-like derivatives laws & won't for **years**
- Plus, 3 comprehensive reviews show no current conflicts:
  - CFTC General Counsel's office
  - European Commission
  - Financial industry
- CFTC cannot afford to wait years before acting simply to avoid the **possibility** of future conflicts
  - If they materialize, CFTC & foreign jurisdictions can work them out as they have with Japan re clearing

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Claimed competitiveness concerns are exaggerated, nonexistent or already addressed

- Claimed competitiveness concerns are speculative
- The CFTC has already accommodated industry requests to level the playing field in its cross-border guidance
  - For example, a change now under consideration would ensure similar regulatory treatment regardless of whether a firm chooses to deal in swaps through overseas branch-offices or subsidiaries (provided the branch is a bona fide foreign-based operation)
- Other concerns have been addressed in the further guidance
- In light of these actions, any additional concessions due to self-interested claims of competitiveness would be unwarranted and unacceptably subordinate the legal requirement to protect the US financial system and taxpayers

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Cross Border derivatives activities have already cost the U.S. a great deal

- **Shipping jobs, businesses & revenue overseas, but risk & liabilities from foreign operations stay in/come back to the U.S.:**
  - Bear Stearns: Cayman affiliates operating in New York with swaps desk in London
  - Lehman Bros: swaps book run through London (G)*
  - AIGFP: French affiliate operating in London (G)
  - Citigroup: Cayman affiliates operating in London (G)
  - JPMorgan: "London Whale" = 'nuf said (G)
  - LTCM: Cayman affiliates operated in London

*involved guarantees by U.S. corporate parent or U.S. affiliate

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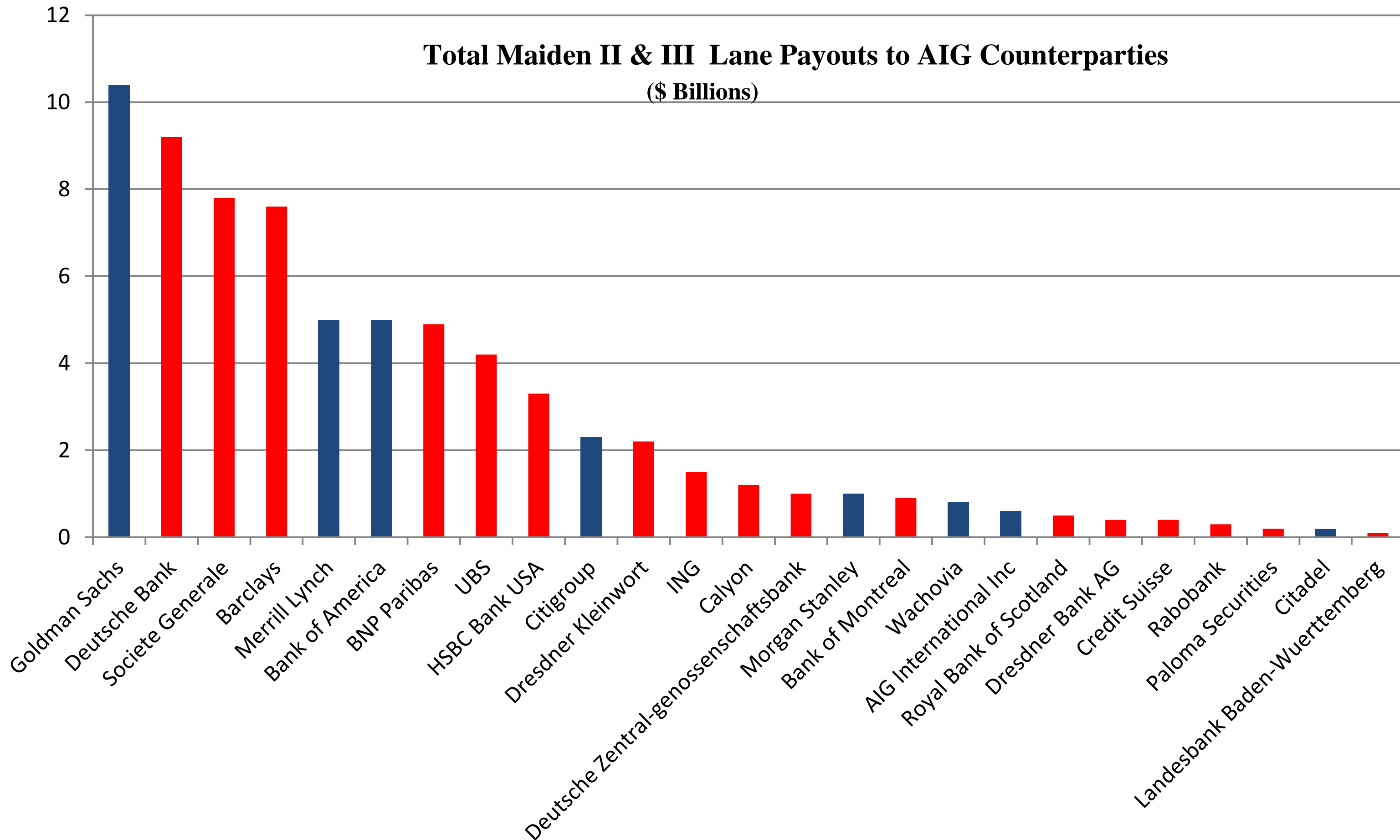
AIGFP risk came home to the U.S.

(blue U.S., red European)



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Not Just AIG: Citigroup

- Citigroup sponsored several Cayman-incorporated SIVs -- essentially small banks funded with commercial paper, with no capital requirements.
- Nominally "bankruptcy remote", but with implicit support from Citigroup.
- SIV commercial paper was widely held by MMFs.
- In late 2007 Citigroup was forced to take $59B in assets, from 7 SIVs, onto its balance sheet to avoid asset fire sales and reputational loss.
- The associated write-downs reduced the bank's capital and began a long-term run on the bank

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Not Just AIG: JPMorgan "Whale"

- **London-based JPM** Chief Investment Office made huge, high risk derivatives bets
  - Risk evaluation was manipulated and risk limits were routinely disregarded.
- **NY-based JPM** suffered losses of $6.2+ billion
  - No one in senior management, risk, legal or compliance were aware of the risks or liabilities being assumed by derivatives positions

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Global Dealers Are Disasters Waiting to Happen

- Global dealers are so big and so sprawling, it is only a matter of time before there are more disasters that require more U.S. bailouts
  - Moreover, these global banks operate in so many parts of world, shifting business from one place to another takes but a **keystroke**
- They are structured & staffed **by design** for regulatory arbitrage & today's virtual markets make that easy
- That is why the law requires the CFTC to impose strong, effective cross border regulations

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Dealer Size & Global Scope Make Cross Border Guidance Critical

- U.S. banks' dealer activities truly global
- JPMorgan Chase: world's biggest bank
  - $2.3 trillion in assets U.S. accounting, $3.75 trillion international accounting (conservative numbers)
  - More than 250,000 employees worldwide
  - Operates in more than 60 countries
  - Has thousands of legal entities worldwide
    - Little cost, less time can have legal entities anywhere, doing almost anything

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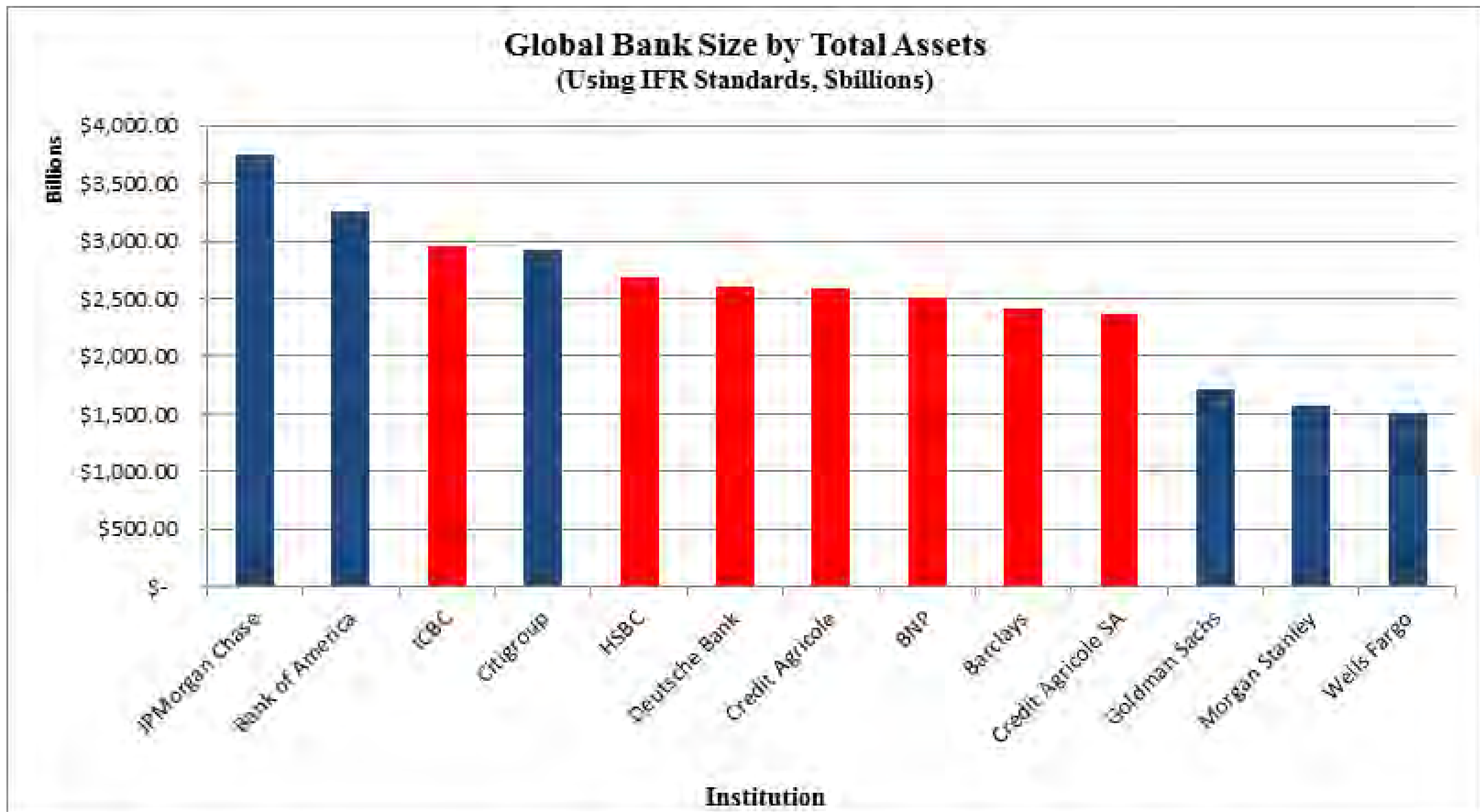
Global Bank Size By Total Assets

Largest banks in the world (blue U.S., red European)



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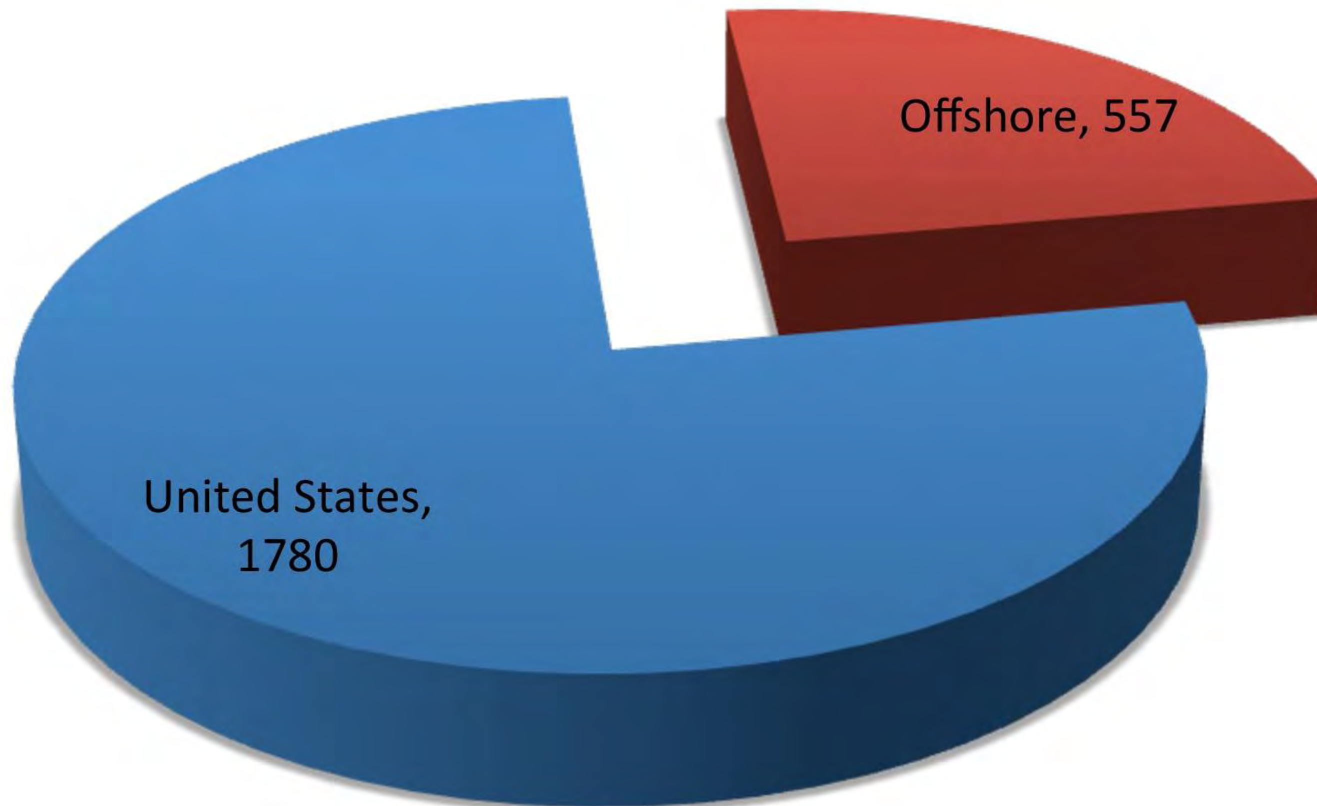
JP Morgan Subsidiaries: Domestic* vs. Offshore



*To avoid a misleading impression, the domestic number excludes 656 subsidiaries (all JPM Plymouth Park Tax Services, LLC entities) because they appear to be shell companies that exist solely to hold delinquent property tax liens used to foreclose on homes in the U.S..

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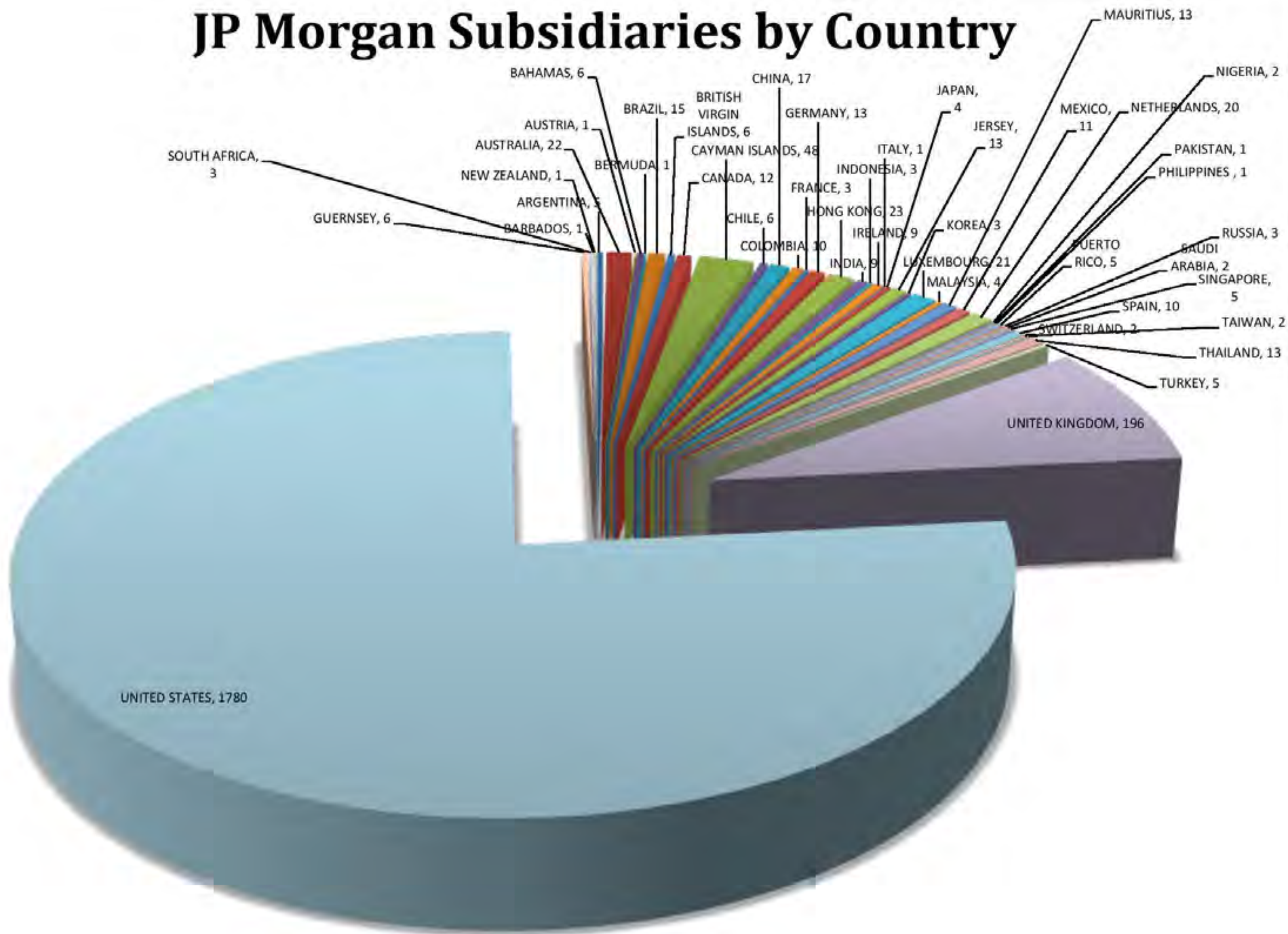

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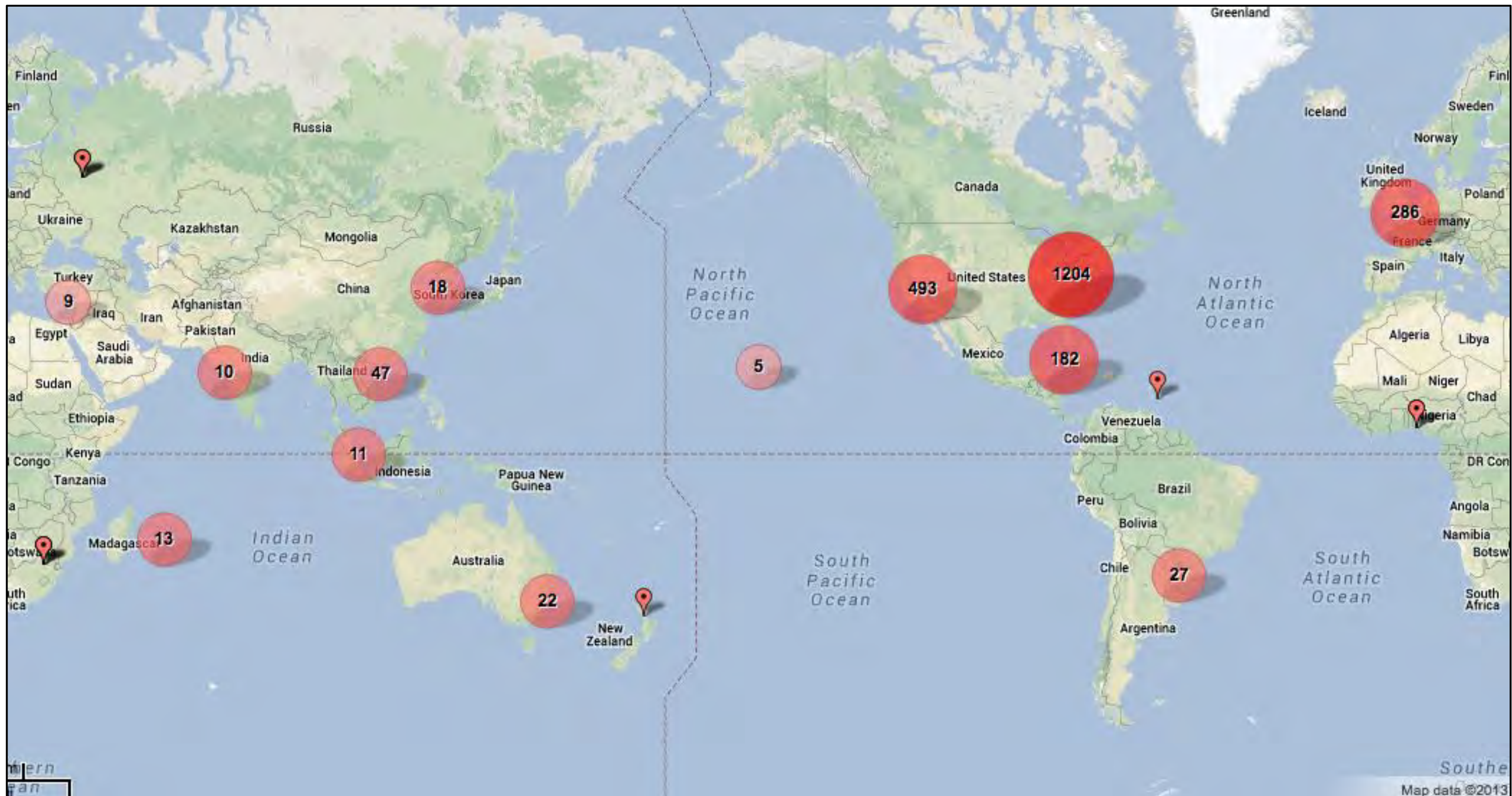
JP Morgan Global Operations



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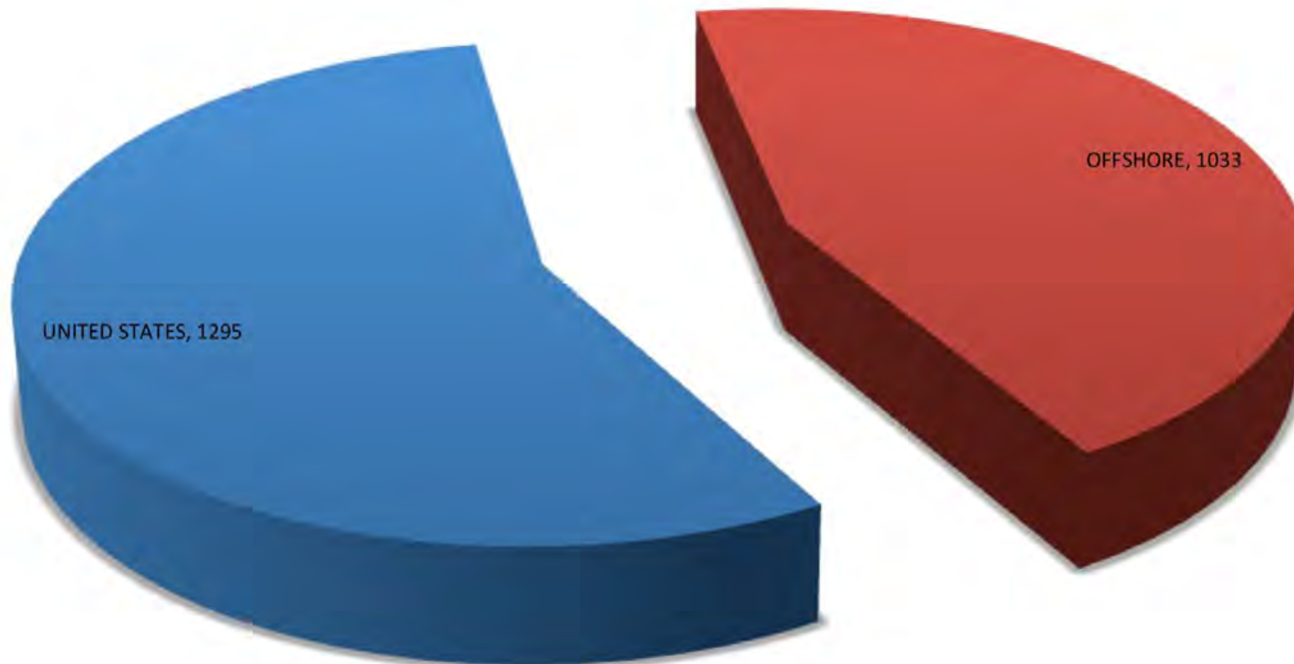
Bank of America Subsidiaries Domestic vs Offshore



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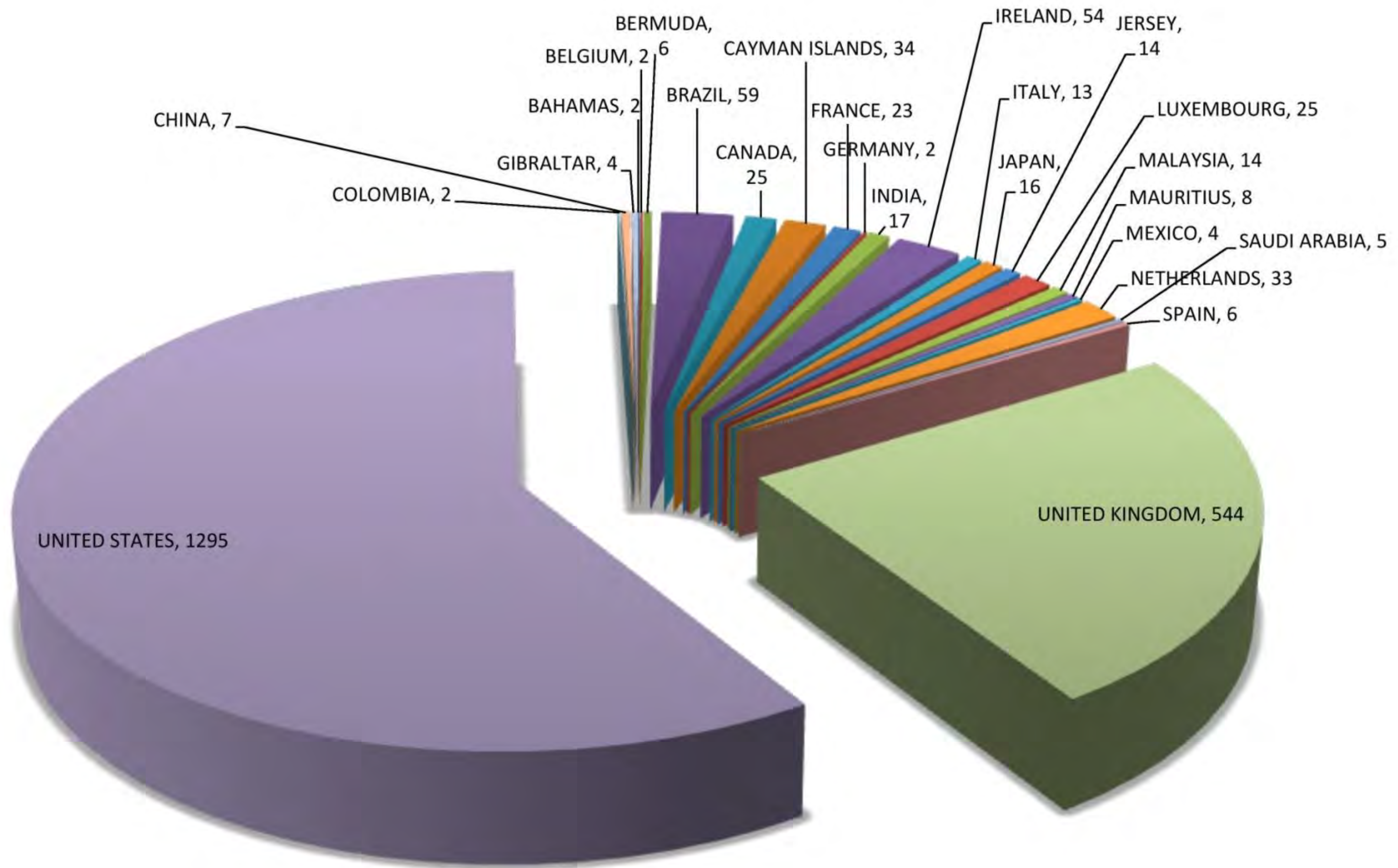

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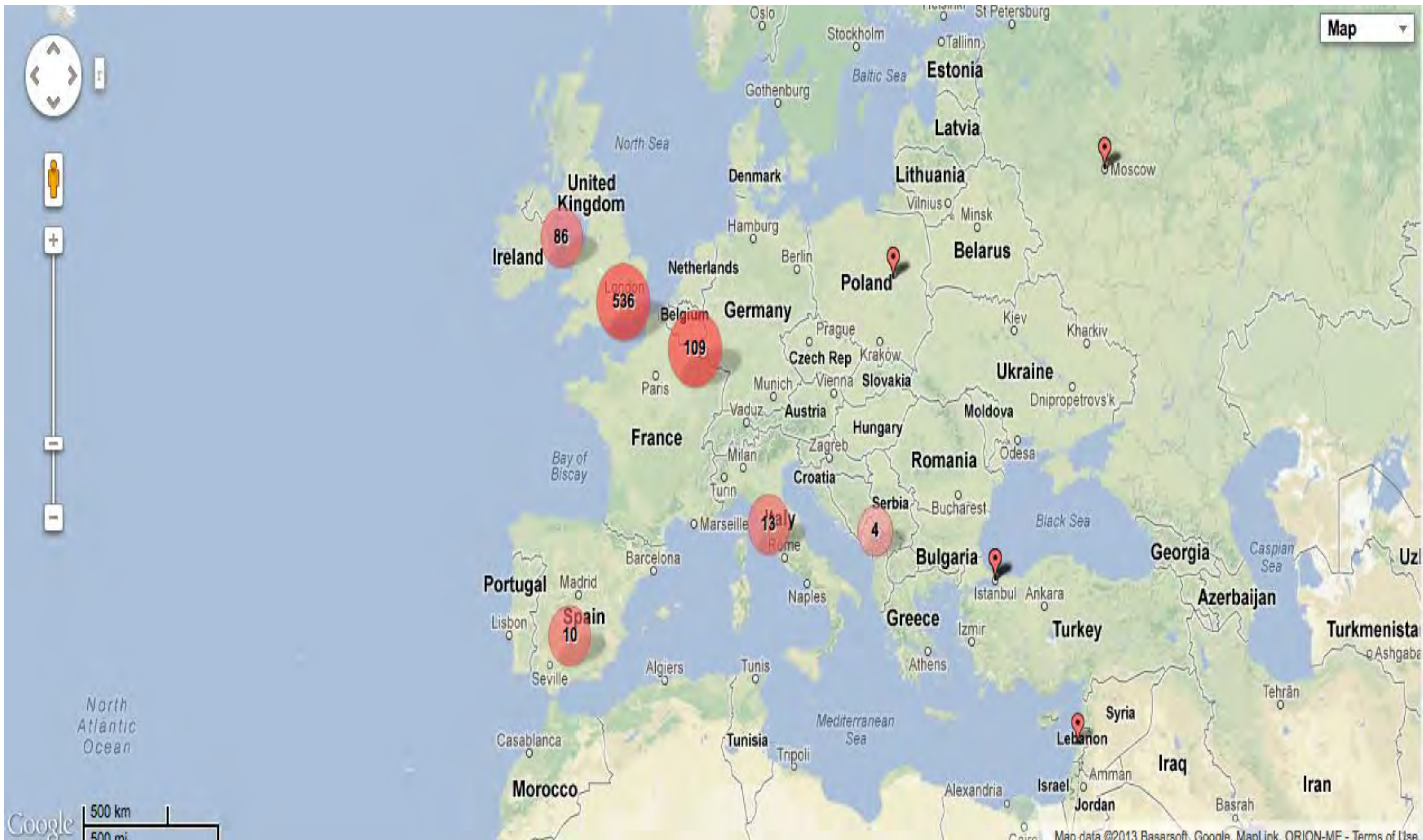
Bank of America's European Operations



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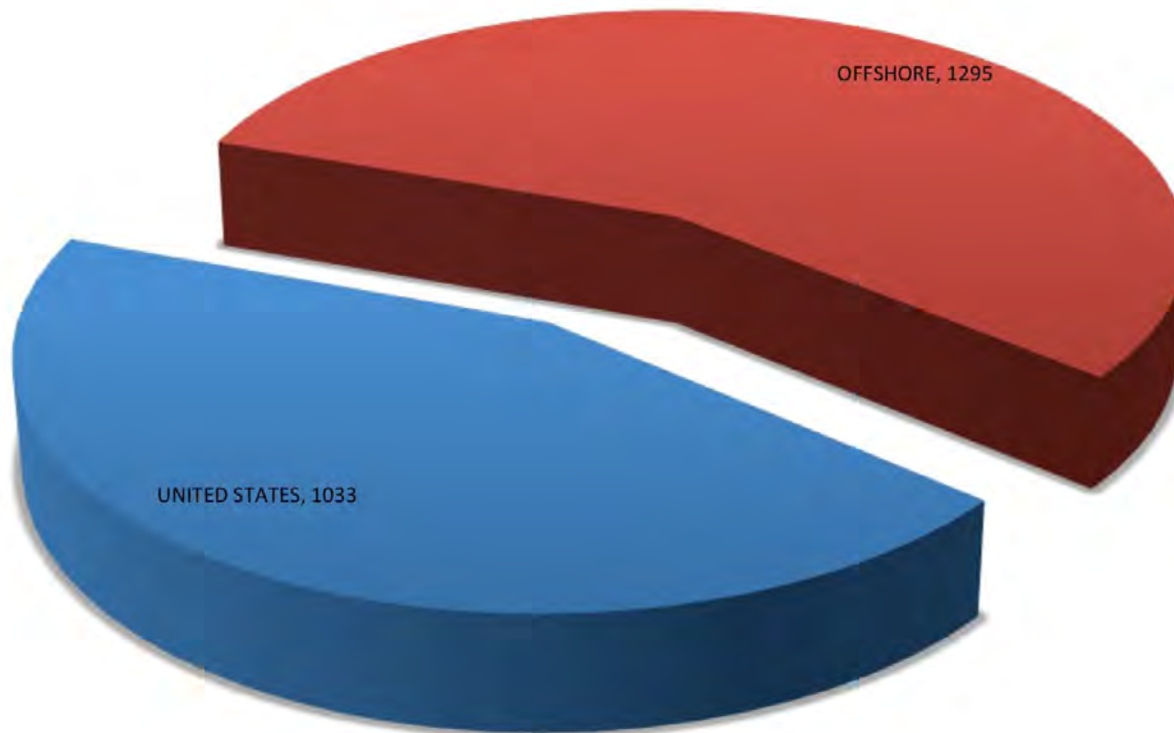
Goldman Sachs Subsidiaries Domestic vs Offshore



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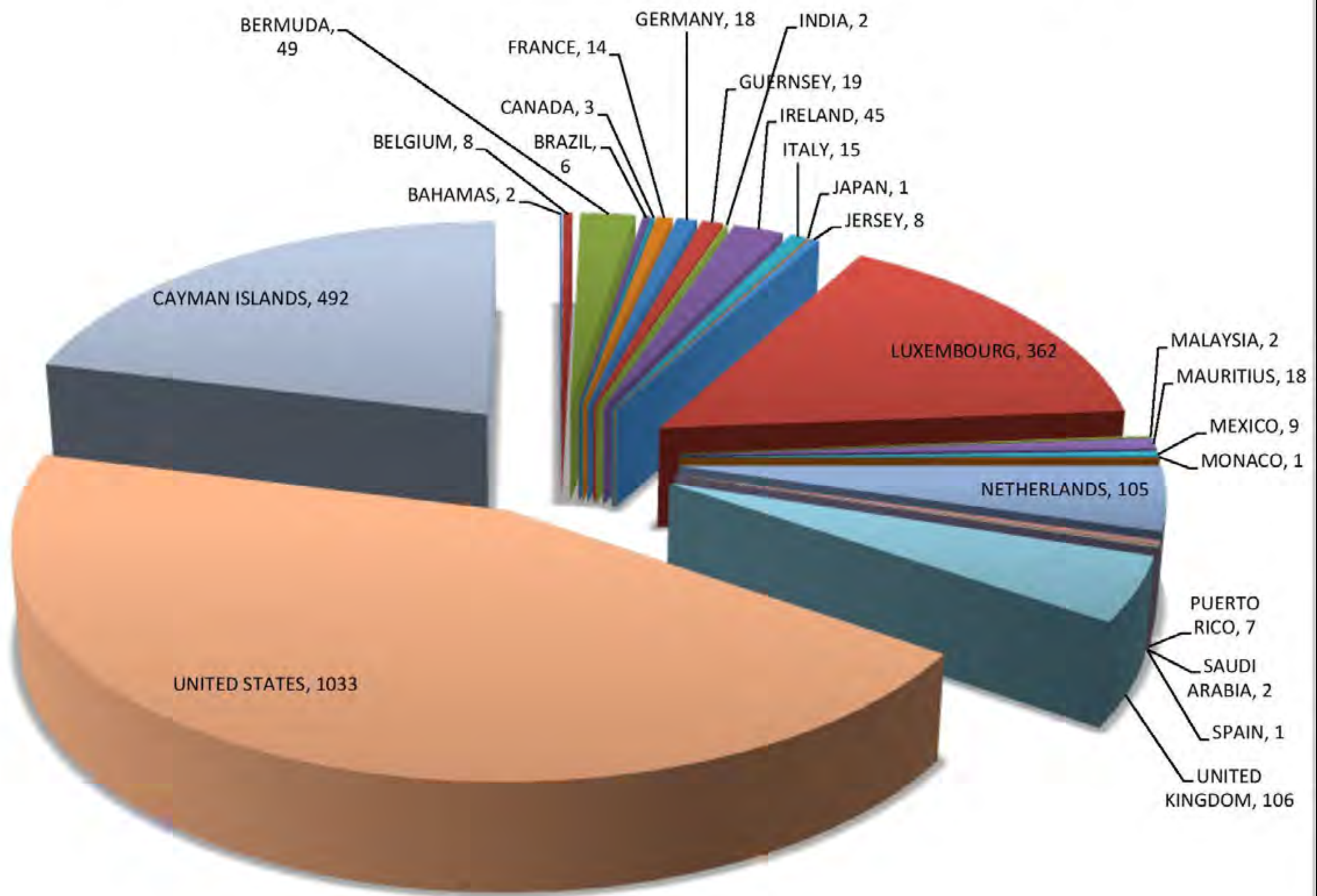

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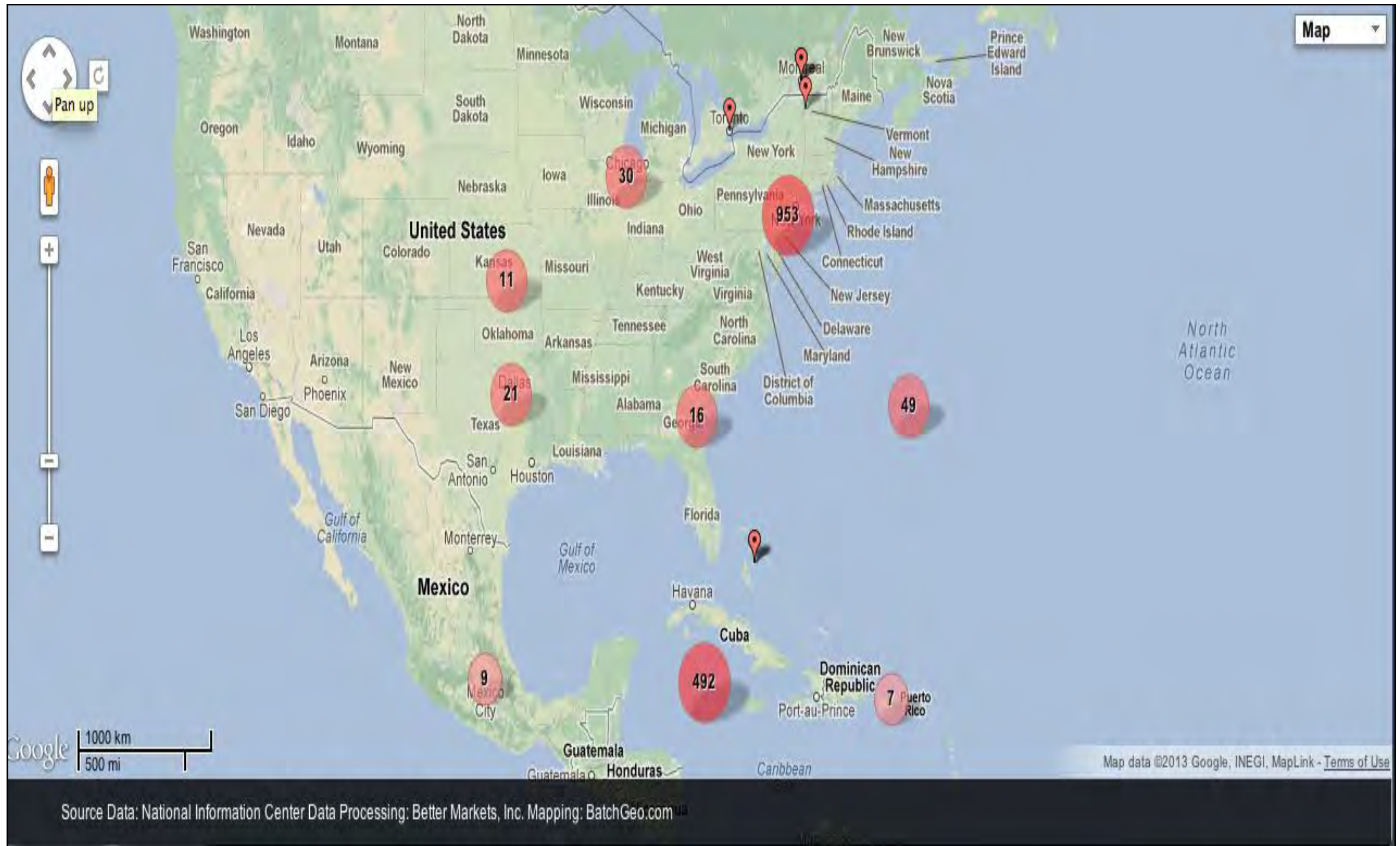
Goldman's North America Operations



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Global banks are experts at moving business activities anywhere in world

AMERICAN BANKER

U.S. Banks Spawn 10,000 Units to Cut Taxes, Avoid Regulation

Bloomberg News
JUL 23, 2012 4:06pm ET

The biggest U.S. banks created more than 10,000 subsidiaries in the past 22 years as they expanded, using legal structures to pay lower taxes and escape tighter regulation, according to a Federal Reserve study.

JPMorgan Chase & Co., the largest U.S. lende[...] Group Inc., Morgan Stanley and Bank of America [...] Federal Reserve Bank of New York shows. Citigroup [...]

Critics including Thomas Hoenig, a Federal Deposit Insura[...] are too complicated to manage. The 2010 Dodd-Frank Act [...] largest banks, if they get into trouble, can be wound down [...] system. U.S. Senator Sherrod Brown has proposed legisla[...]

"When regulators are left to curtail the risk of trillion- dollar [...] know that too big to fail is also too big to manage" said Brown, an Ohio Democrat and member of the Senate Banking Committee.

The 1999 repeal of the Depression-era Glass-Steagall Act was the main catalyst for the biggest banks getting bigger, the Fed study concluded. The assets of the largest lenders have since tripled to $15 trillion. Hoenig has called for reinstating Glass-Steagall, which separated investment and commercial banking, while Brown's proposal would limit asset size.

Legal Status

Morgan Stanley and Goldman Sachs, whose main business is investment banking, have thousands more subsidiaries than some of their bigger peers, who focus more on commercial and consumer lending. The two New York-based firms changed their legal status to bank holding companies during the height of the financial crisis in 2008 to access unrestricted Fed funds.

Goldman Sachs and Morgan Stanley each have about 3,000 legal units, more than double the 1,366 entities controlled by Wells Fargo & Co., according to the Fed study. San Francisco- based Wells Fargo has roughly 40 percent more assets than Goldman Sachs and 75 percent more than Morgan Stanley.

The biggest U.S. banks created more than 10,000 subsidiaries in the past 22 years as they expanded, using legal structures to pay lower taxes and escape tighter regulation, according to a Federal Reserve study.

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"All the News That's Fit to Print"

The New York Times

Late Edition

Today, partly sunny, milder, high 46. Tonight, turning mostly cloudy, but not as cold, low 35. Tomorrow, cloudy, showers arriving, high 45. Weather map appears on Page D8.

VOL. CLVII . . No. 54,231 © 2008 The New York Times New York, Tuesday, May 21, 2013 $1.25

BILLIONS IN TAXES AVOIDED BY APPLE, U.S. INQUIRY FINDS

Global Web of Subsidiaries Shields Profits – Executives to Testify in Defense

WASHINGTON — Even as Apple became the nation's most profitable technology company, it avoided billions in taxes in the United States and around the world through a web of subsidiaries so complex it spanned continents and went beyond anything most experts had ever seen, Congressional investigators disclosed on Monday.

The investigation is expected to set up a potentially explosive confrontation between a bipartisan group of lawmakers and Timothy D. Cook, Apple's chief executive, at a public hearing on Tuesday.

Congressional investigators found that some of Apple's subsidiaries had no employees and were largely run by top officials from the company's headquarters in Cupertino, Calif. But by officially locating them in places like Ireland, Apple was able to, in effect, make them stateless — exempt from taxes, record-keeping laws and the need for the subsidiaries to even file tax returns anywhere in the world.

"Apple wasn't satisfied with shifting its profits to a low-tax offshore tax haven," said Senator Carl Levin, a Michigan Democrat who is chairman of the Senate Permanent Subcommittee on Investigations that is holding the public hearing Tuesday into Apple's use of tax havens. "Apple successfully sought the holy grail of tax avoidance. It has created offshore entities holding tens of billions of dollars while claiming to be tax resident nowhere."

Thanks to what lawmakers called "gimmicks" and "schemes," Apple was able to largely sidestep taxes on tens of billions of dollars it earned outside the United States in recent years. Last year, international operations accounted for 61 percent of Apple's total revenue.

Investigators have not accused Apple of breaking any laws and the company is hardly the only American multinational to face scrutiny for using complex corporate structures and tax havens to sidestep taxes. In recent months, revelations from European authorities about the tax avoidance strategies used by Google, Starbucks and Amazon have all stirred public anger and spurred several European governments, as well as the Organization for Economic Cooperation and Development, a Paris-based research organization for the world's richest countries, to discuss measures to close the loopholes.

Still, the findings about Apple were remarkable both for the enormous amount of money involved and the audaciousness of the company's assertion that its subsidiaries are beyond the reach of any taxing authority.

"There is a technical term economists like to use for behavior like this," said Edward Kleinbard, a law professor at the University of Southern California in Los Angeles and a former director at the Congressional Joint Committee on Taxation. "Unbelievable chutzpah."

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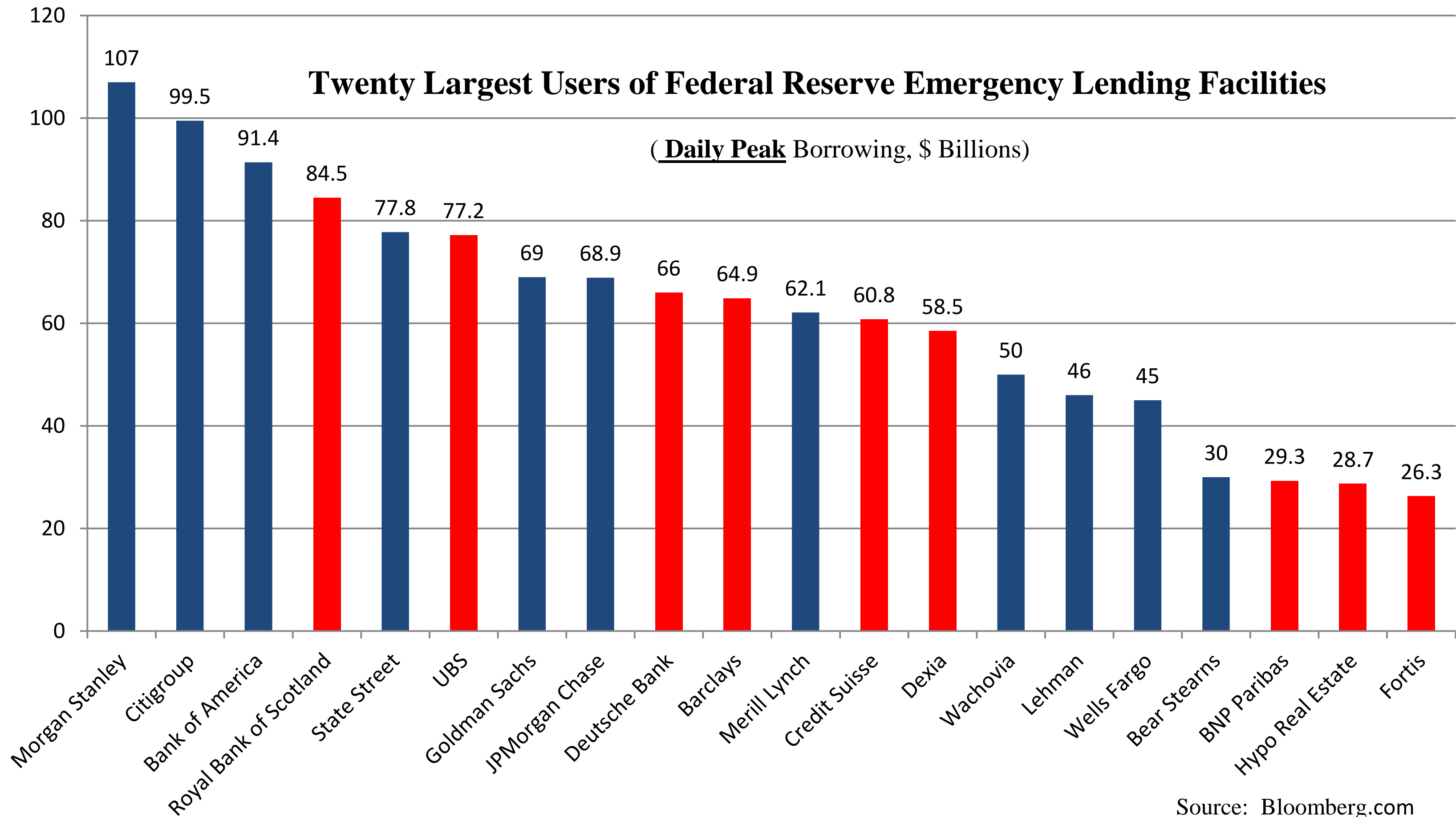
EU banks required U.S. bailouts

(blue U.S., red European)



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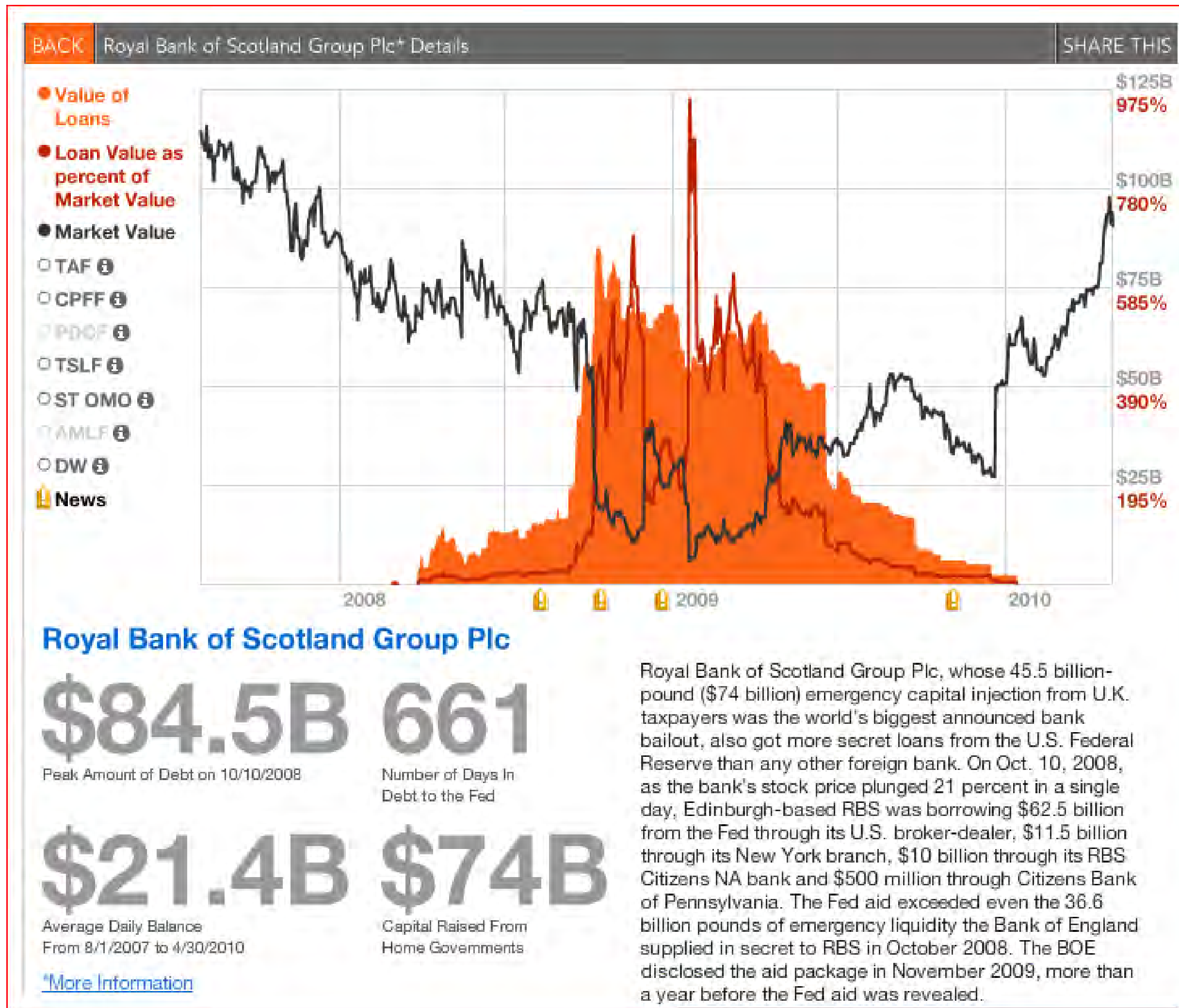
Fed lending to Royal Bank of Scotland (RBS)



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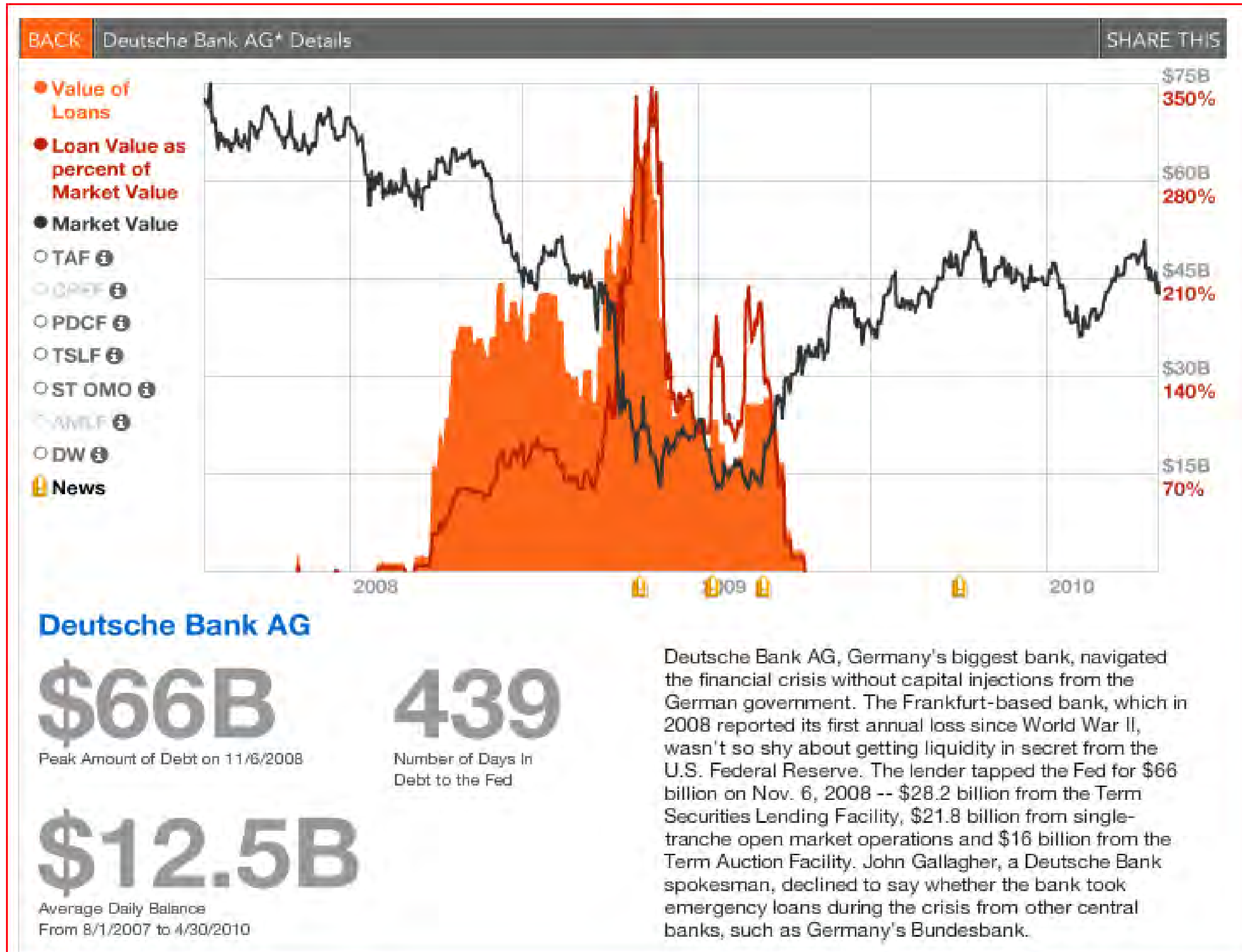
Fed lending to Deutsche Bank



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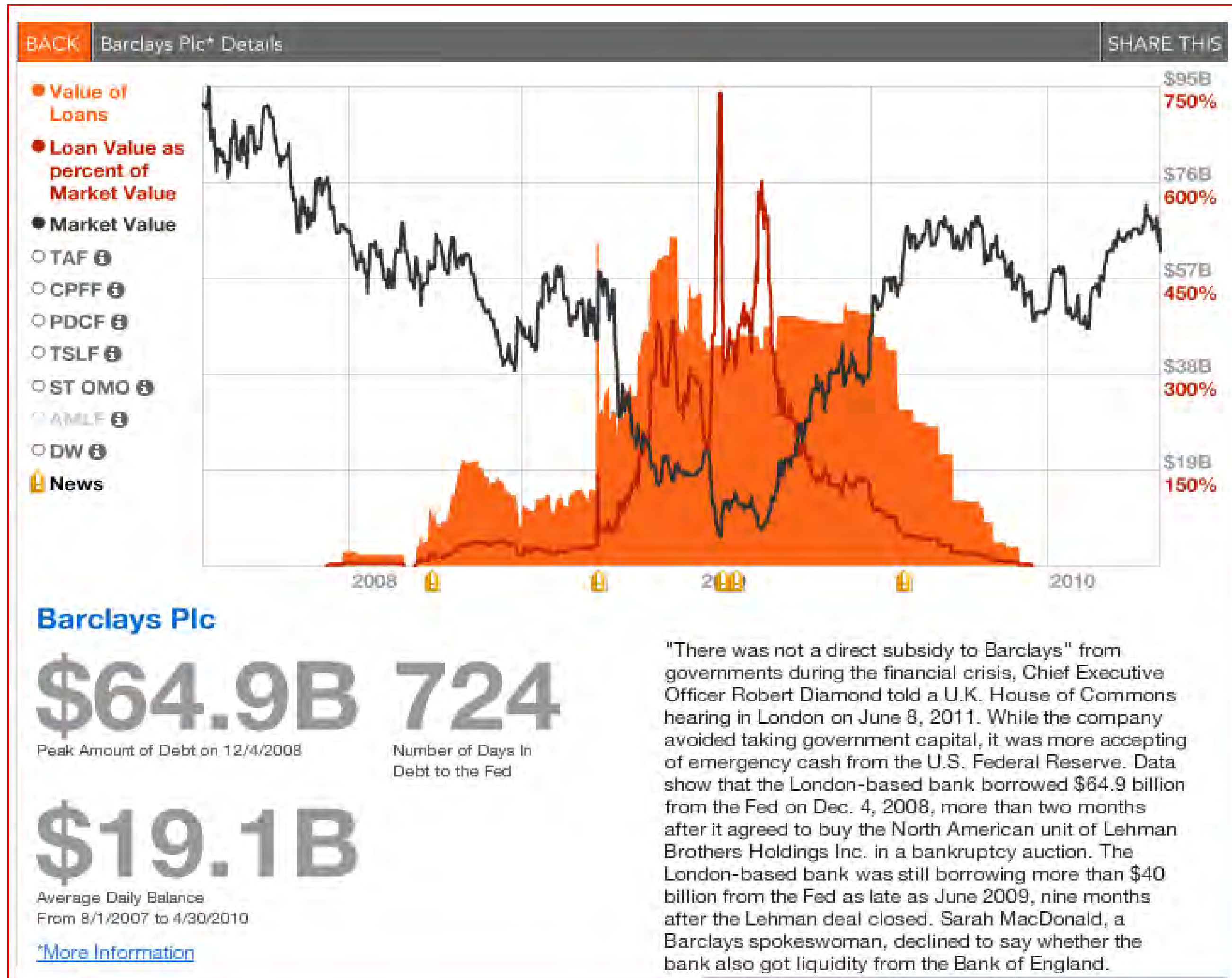
Fed lending to Barclays



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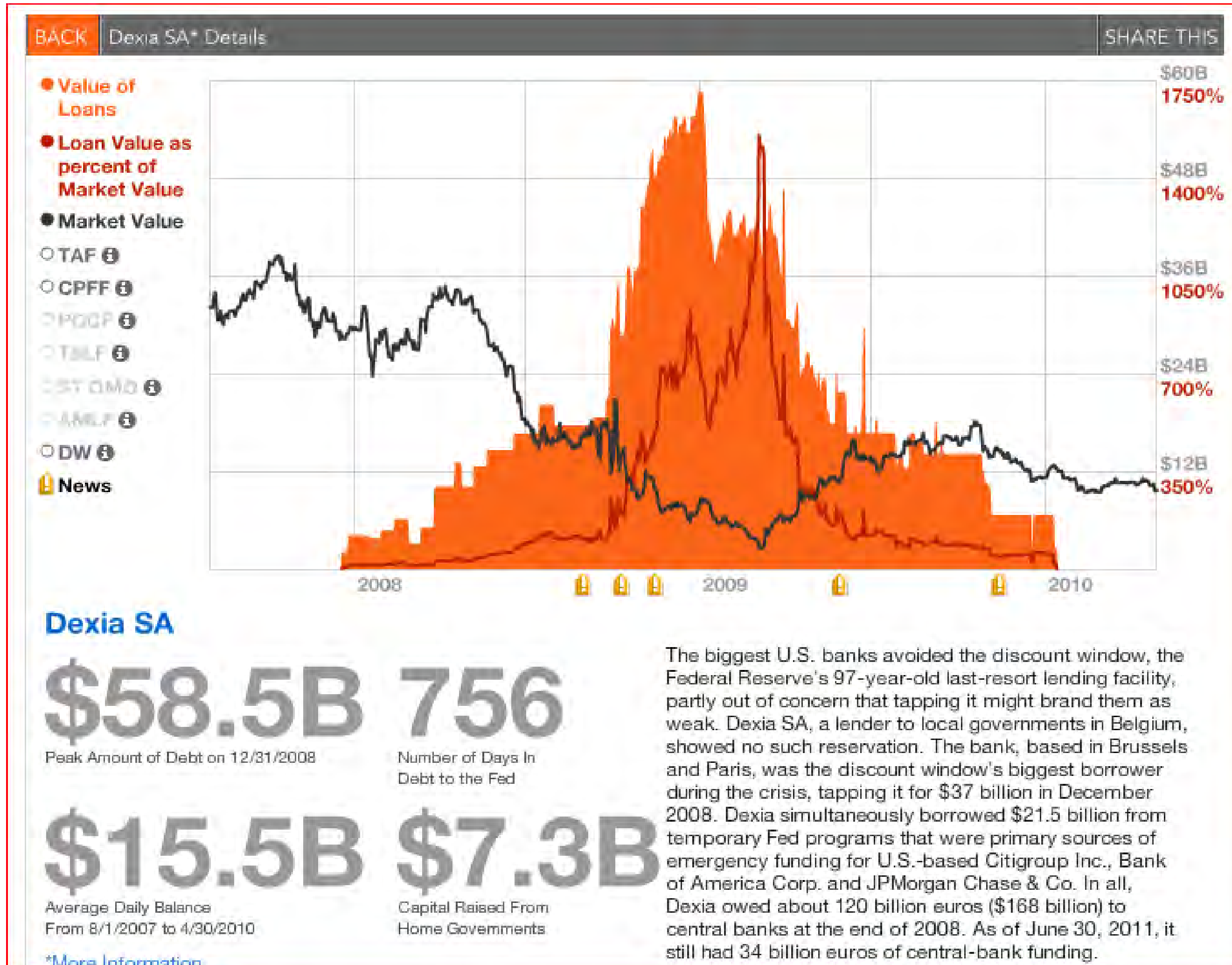
Fed lending to Dexia SA



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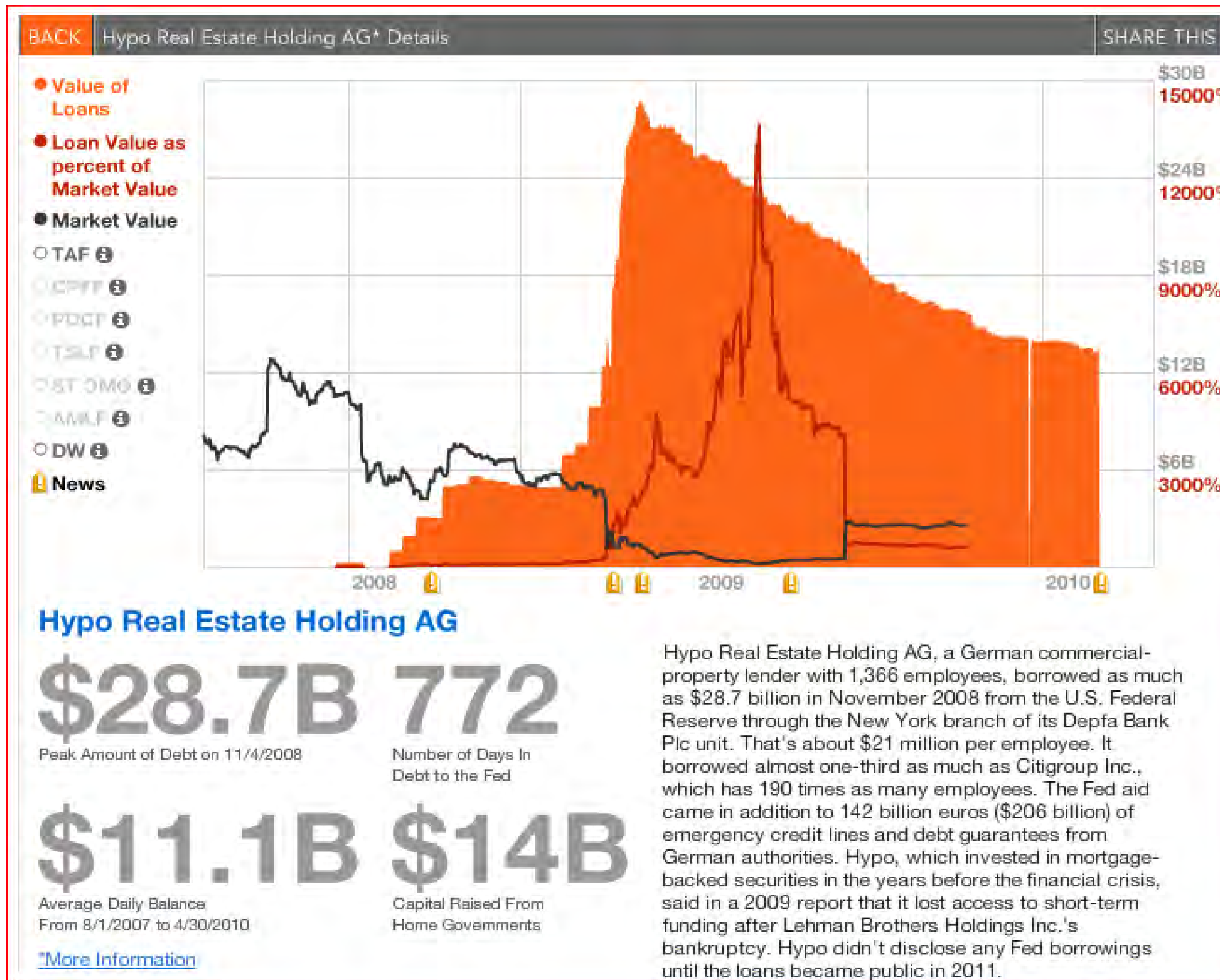
Fed lending to Hypo Real Estate Holding



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But even that's not all: Costs of Foreign Regulator Failures have been staggering

- **In addition** to (1) the AIG-like cross border bank/dealer disasters that have come back to cost the U.S. **and** (2) the trillions in Fed bailouts,
  - There was **also** massive, widespread and very costly failure of foreign financial regulation even of their own banks and dealers – **never mentioned**
- The result was many EU banks were nationalized or otherwise bailed out by their own governments during the crisis

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EU bank regulation totally failed
Foreign depositors, taxpayers and treasuries

EU Banks rescued by their governments during the crisis

U.K.	Germany
Northern Rock *	West LB
Royal Bank of Scotland *	Landesbank Baden Wurttemberg
Lloyds Banking Group	IKB
Bradford and Bingley *	Hypo Real Estate *
HBOS	Nord LB
	Commerzbank AG
Belgium	**Netherlands**
Dexia *	
KBC Group	ING
Fortis	SNS REAAL
France	**Sweden**
Caisse d'Espargne/Bansque Populaire	Carnegie Bank *
Ireland	**Switzerland**
Anglo Irish Bank *	UBS

Source: Centre for European Policy Studies (2010), Bank State Aid in the Financial Crisis, October

*government majority ownership

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£0.80
Monday 13.10.08
Published in London and Manchester
guardian.co.uk

theguardian

Banks to get £46bn injection from taxpayers to stay afloat

Fears that bill may rise to £75bn

Jill Treanor
Larry Elliott
Nicholas Watt

The cost to the taxpayer of bailing out Britain's weakest banks will escalate today when the government announces an injection of more than £40bn into the country's struggling high street lenders.

In a sign of the deepening financial crisis, the government is standing by to take majority stakes in Royal Bank of Scotland and HBOS, owner of the country's biggest mortgage lender Halifax, and smaller stakes in Barclays and Lloyds TSB.

Top executives from the big banks were in discussions with the Financial Services Authority, Treasury and Bank of England last night about how they would participate in the bail-out, originally intended to allow for £25bn to be injected into banks immediately, with a further £25bn later.

But RBS and HBOS are likely to use £25bn alone, and there were estimates last night that the total bill could rise to £75bn. The three-part package also includes £200bn of fresh funds for interbank lending and a

Sir Fred Goodwin could be ousted as chief executive of RBS, in which the government is ready to take a majority stake

tion of making a statement before markets open at 8am. Sources said yesterday that the government would assume a larger than expected control of banks after the dramatic fall in their share prices. They cite the example of RBS, which is now worth £12bn but needs at least £20bn to help it recapitalise. "On these figures we are suddenly the majority shareholder," one government source said.

HBOS, which had a market value of £6.5bn on Friday, could need to raise up to £12bn and Lloyds TSB £5bn, with Barclays needing up to £9bn. The terms of the fund-raisings are complex. Some of the shares may be ordinary shares, which give voting rights, and some could be preference shares, which do not. HBOS, for instance, could raise around £9bn in ordinary shares and a further £3bn in preference shares, while RBS could raise £15bn in ordinary shares and £5bn in preference shares.

The rise in the size of the capital injections being demanded by the FSA over the weekend surprised some banks. But it is thought that the regulator is determined to draw a line under concerns about whether the capital cushions held by the banks are enough to prevent them collapsing.

The government insisted it was not taking control of banks in the long term. "This is not nationalisation. This is the banks coming to us requesting capital," the government source said. "If we are going to take a significant share of these banks, we have got to protect the interests of the taxpayer. But we have no intention

Europe follows Brown plan for survival

Ian Traynor Paris
Larry Elliott Washington

Germany, France, Italy and a further 12 European countries last night unveiled a "comprehensive" plan for salvaging their banking systems from potential ruin, as panicked European leaders met to try to ward off more financial meltdown before the markets reopen today.

An emergency summit in Paris of the 15 countries using the euro single currency was encouraged by Gordon Brown to adopt the rescue plan he launched last week as the template for an increasingly global approach to the financial crisis.

Yesterday's summit in Paris followed a frenetic weekend of activity in Washington, in which the IMF, the World Bank, the G7 club of rich western nations and the broader G20 group, all called for urgent and coordinated action.

Dominique Strauss-Kahn, managing director of the IMF, warned that the global financial system was "on the brink of systemic meltdown".

The IMF's main policy committee issued a statement saying that it "recognises that the depth and systemic nature

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FINANCIAL TIMES

Tuesday January 20 2009 | £1.80

Good morning, Mr President

Inauguration day: the world wakes up to Obama's Washington

Analysis Page 11, **Editorial Comment** Page 12, Plus **Special report**

Crunch time Nationalise the banks now, says Christopher Wood Page 36

Newspaper of the year

World Business Newspaper

News Briefing

C4 chief seeks a 'best for Britain' solution

Diageo reviews plans

Art market crunch

S&P cuts Spain's rating

Russian lawyer killed

Gaza rebuilding row

Indian recall revolution

Rouble devaluation off

Turkey pipeline threat

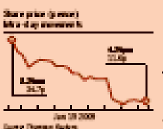
RBS plunges despite lifeline

Fears of state takeover after 67% share fall

Treasury unwilling to take on balance sheet

Prime minister Gordon Brown and chancellor Alistair Darling announce the second rescue plan for the banking industry

RBS suffers on the markets



£28bn

RBS set for biggest loss in UK corporate history

67%

Slide in the bank's shares to a 23-year low of 11.6p

PM's rebuke

'Today's write-off is for irresponsible losses in US subprime markets that partly derive from the acquisition of ABN'

Stephen Hester

'RBS leveraged itself too much in the good times – the ABN acquisition was an element in that...'

RBS chief executive

Bank of England

Treasury gives go-ahead to 'print money'

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FINANCIAL TIMES SEPTEMBER 15/SEPTEMBER 16 2012 ★ 3
Northern Rock: five years on

Rock's fall has left millions in a hard place

Banking

Jonathan Eley, Elaine Moore and Tanya Powley look at how Northern Rock's dramatic failure affected investors, savers and mortgage borrowers

When Northern Rock reported half-year results in July 2007, it was able to boast that first-half net lending was £10.7bn, a new record and 18.9 per cent of all UK net lending. "The medium-term outlook for the company is very positive," said chief executive Adam Applegarth, announcing a 30 per cent increase in the interim dividend. Less than two months later, the company became the victim of the first run on a UK bank for over a century, and within a year it had collapsed into the arms of the state. More turmoil followed in 2008, when Lloyds and Royal Bank of Scotland were partially nationalised.

Investors

Northern Rock's rapid fall from grace confounded investors. The first thing to go was the dividend that was "deferred" – indefinitely, as it turned out. Others weren't far behind. In 2007, the banking sector accounted for 21 per cent of all UK dividend income, according to data from Capita Registrars. By 2011 it was 9.7 per cent.

Although Barclays, HSBC and Standard Chartered still pay dividends, they have been "rebased" to lower levels. Any distributions to shareholders remain firmly off the agenda at RBS and Lloyds, so long as they remain wards of the state.

Share prices have also slumped – Barclays is down from over £7 to just over £2, while Lloyds shares peaked at over £5 but now trade at around 30p, half the price at which the government acquired its 41 per cent stake. But at least they're still trading; investors in Northern Rock are unlikely to receive any meaningful compensation for the bank's nationalisation.

Despite the turmoil, bank shares remain heavily traded by private investors. "Lloyds shares have been our top buys and sells by volume since 2009," said Stuart Welch, chief executive of TD Direct Investing, a leading online stockbroker. "In 2009 and 2010, it was all about traders. Bank shares were quite volatile and there was a pattern of rising and falling," he added. "From an investor's point of view, banks remain a recovery story. They expect – or hope for – some kind of turnaround in the long term."

Paul Kavanagh, a partner at stockbroker Killik, says there are signs of such a turnaround. "Historically, bank shares have traded at price-to-book-value ratios of 1 to 1.5. They're at about 0.6-0.7 now. Another couple of years of steady, good performance and I think that gap will start to close."

Immediate prospects are better in the subordinated debt market, which is dominated by permanent interest bearing shares (Pibs), a form of perpetual subordinated bond considered ideal for risk-averse income seekers and widely held by private investors. But in May 2009, Bradford & Bingley became the first UK bank in modern history to miss an interest payment on its debt.

Lloyds was also forced to suspend interest payments on its preference shares because of state aid rules.

Savings

The past five years have been disastrous for savers as low interest rates and relatively high inflation have eroded the purchasing power of cash. The only consolation, say savings experts, is that it could have been much worse.

With access to the wholesale money markets severely constrained and more stringent capital requirements on the way, banks and building societies have had to compete fiercely for retail deposits. They've done this by using short-term bonuses.

Advisers say that bonus rates offer customers the only chance to keep pace with rising prices, so long as they remember to switch once the bonus period ends.

"Savers have clearly lost out since Northern Rock collapsed," said Mark Giddens at accountancy firm UHY Hacker Young. His research found that savers are losing nearly £18bn a year because of record low interest rates and the higher cost of living.

"In the old days, interest rates ran above inflation, but I think the situation for the next few years will remain as it is now."

Reports suggest that the Bank of England is considering a further cut in interest rates to 0.25 per cent, which could lead to a knock-on reduction in baseline cash savings rates.

According to research by Moneyfacts, savers who kept their money in easy access accounts were earning an average return of more than 4 per cent in 2007. Today they earn just over 1 per cent – and inflation is higher too.

The best return available in an easy-access cash account is 2.9 per cent from ING Direct, which includes a 2.25 per cent bonus.

The number of providers has fallen too. Before the financial crisis the best-buy savings tables were dominated by international banks, including Icelandic banks offering 6 per cent plus returns.

However, money put into foreign banks operating here is now more likely to be covered by the UK's Financial Services Compensation Scheme than in 2007.

The FSCS was set up in 2001 and would have protected up to £35,000 of every individual's money saved in Northern Rock, regardless of government guarantees. Following the crisis, the amount protected was increased, first to £50,000 and then £85,000 and the scheme has worked hard to make itself more visible to make savers feel secure. All banks and building societies must now state whether or not they are members of the FSCS and there are plans to create a Europe-wide compensation scheme, though it is not yet clear whether or not the UK will be included.

Mortgages

Getting a mortgage has become significantly harder in the five years since the Northern Rock crisis, with lenders becoming increasingly risk averse.

Banks and building societies have stricter acceptance criteria and have cut the deals available drastically, particularly for borrowers with small deposits.

Former Northern Rock chief executive Adam Applegarth

Five years ago there were thousands of low-deposit mortgages offered by lenders, including hundreds of deals for borrowers with no deposit, with some banks – such as Northern Rock – offering 125 per cent loan-to-value mortgages.

Today, the picture is very different. While there were 238 mortgages available for borrowers with no deposit in September 2007, there are now only five.

Those with a 5 per cent deposit had a choice of 395 deals five years ago but just 67 today, according to Moneyfacts.

"The biggest immediate effect of the Northern Rock crisis was that high street lenders severely restricted loan-to-values as a result of the money supply drying up," said Nigel Bedford, senior partner at Largemortgageloans.com, the mortgage broker. "What they did have to lend, they logically lent to the lowest risk customers."

238
100 per cent mortgage deals available in Sept 2007

5
100 per cent mortgage deals available in Sept 2012

The situation worsened the following year when Lehman Brothers collapsed, and the securitisation market effectively closed. Mark Harris of SPF Private Clients, the mortgage broker, believes this was the final straw for the mortgage market. The total number of mortgages approved fell from about 3.6m in 2007 to just under 1m in 2009.

"In the aftermath it was difficult to borrow even 75 per cent loan-to-value," noted Bedford. "When the world didn't end and every bank didn't collapse, we gradually saw lenders return to the market and offer higher loan-to-values."

The outlook is slowly improving for borrowers with small deposits. The number of 95 per cent loan-to-value deals has risen from just nine in 2009 to 67 today. However, experts believe the market has seen the last of risky 125 per cent mortgage deals – although most observers consider this to be no bad thing.

But there remains a big divide in today's mortgage market. The reduction of the Bank of England base rate to 0.5 per cent benefited many existing homeowners who took out variable rate deals, which track the base rate, and saw their monthly payments fall. Lower wholesale funding costs in the past year, driven by quantitative easing and the announcement of the government's Funding for Lending scheme (FLS), has resulted in historically low-priced fixed-rate deals for new homebuyers and movers. Low-risk borrowers can now secure long-term fixed-rates of below 3 per cent.

Higher-risk borrowers, those with small deposits and first-time buyers, continue to struggle. New rules proposed by the Financial Services Authority to curb irresponsible lending resulted in lenders imposing stricter criteria, making it harder for those with interest-only or self-certification mortgages to move home. "What this means is we have a split population; on one side the fortunate who are not paying much to borrow, and on the other, there is a group that is stuck or simply can't borrow at all," explained Ben Thompson of L&C Mortgage Club.

The outlook appears to be improving. Although it is early days, the FLS, introduced last month to encourage banks to lend to homeowners and small businesses, has already helped lower mortgage costs for some borrowers.

The Bank of England is considering another rate cut

Five years that rocked UK banking

- Sep 13 2007: BBC reveals that Northern Rock asked for help from the Bank of England
- Sep 14 2007: Queues start forming outside Northern Rock branches. Government guarantees deposits
- Feb 18 2008: Northern Rock shares suspended as company is nationalised
- Apr 22 2008: RBS raises £12bn in rights issue
- Sep 15 2008: Lehman Brothers files for Chapter 11 protection, triggering turmoil on world markets
- Sep 17 2008: Lloyds announces takeover of HBOS
- Sep 29 2008: Bradford & Bingley branch network sold to Santander, loan book taken over by government
- Oct 13 2008: Government announces nationalisations of RBS and Lloyds
- Mar 5 2009: Bank of England cuts main lending rate to 0.5%, an all time low
- May 26 2009: Bradford & Bingley defaults on interest payments on subordinated bonds, the first bank to do so
- Dec 17 2010: FSCS raises UK account compensation limit to £85,000
- Nov 17 2011: Virgin agrees to buy 'good bank' of Northern Rock for £747m
- Jul 10 2012: Lloyds says it will sell 632 branches to Co-operative Bank

Source: FT research. Photos: Getty, Reuters. FT graphic

MORE ON THE WEB
Listen to the FT Money team on how the failure of Northern Rock changed savings, borrowings and investment www.ft.com/moneyshow
See our detailed interactive timeline of the Northern Rock saga at www.ft.com/money

UK banks
FTSE All-share banks index
(Chart: 2000–12000; 2007, 08, 09, 10, 11, 12)
Source: Thomson Reuters Datastream

Bravo! Top talent worth applauding.
Henderson Sterling Bond Unit Trust

It takes talent and experience to achieve results. Philip Payne and Stephen Thariyan have spent more than 30 years honing their skills as fixed income fund managers. In April 2009, Philip and Stephen took on responsibility for managing the Henderson Sterling Bond Unit Trust. Since then, they have focused the fund primarily on high quality, investment grade corporate bonds, issued by companies with a strong financial standing and history of healthy profits.

This approach has proven successful as the Henderson Sterling Bond Unit Trust is ranked in the top 10% of funds of its type since Philip and Stephen took on management responsibility for the fund.

Henderson Sterling Bond Unit Trust:
- 3.8% distribution yield and 3.6% underlying yield, paid quarterly
- Expertly managed by Philip Payne and Citywire AAA rated Stephen Thariyan

Past performance is not a guide to future performance. The value of an investment and the income from it can fall as well as rise and you may not get back the amount originally invested. Yields may vary and are not guaranteed. If you are unsure about the suitability of an investment, please contact your financial adviser.

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Foreign financial regulators failed miserably to protect their own taxpayers, depositors, treasuries

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The costs of those failures have been staggering, exceeding GDP

- Because these costs are ongoing, it's impossible to calculate how much these failures will ultimately cost the people of Europe
  - But we know the peak government bailout costs in just one country: the nationalized cost in the UK alone to 2011 was more than $1.15 trillion pounds

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Trillions More in Costs to European Citizens

- Because these banks/dealers were nationalized, their total liabilities have been assumed by the public
  - **Just one** of the five UK nationalized dealer banks' RBS, had total assets (& therefore total liabilities) in 2008 of 2.2 trillion pounds
    - The UK's entire GDP in 2008 was just 1.4 trillion pounds
      - The country's taxpayers have had to assume private liabilities well above their entire GDP

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Foreign financial regulation has failed shamefully in other areas as well

- There has also been massive, wide-spread, multi-year LIBOR rate-rigging throughout the EU by the large dealer derivatives desks
- Plus, there has been massive, wide-spread, multi-year criminal money laundering by Standard Chartered, HSBC and other global bank/dealers, which was also undetected by European regulators
- And, ongoing: ISDAfix markets, FX markets & who knows what other crimes & manipulation going on

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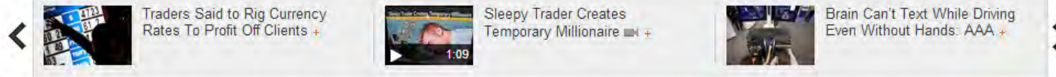

Traders Said to Rig Currency Rates To Profit Off Clients

Sleepy Trader Creates Temporary Millionaire

Brain Can't Text While Driving Even Without Hands: AAA

Traders Said to Rig Currency Rates to Profit Off Clients

By Liam Vaughan, Gavin Finch & Ambereen Choudhury - Jun 11, 2013 7:00 PM ET

June 11, 2013

58 COMMENTS QUEUE

Traders at some of the world's biggest banks manipulated benchmark foreign-exchange rates used to set the value of trillions of dollars of investments, according to five dealers with knowledge of the practice.

> Traders at some of the world's biggest banks manipulated benchmark foreign-exchange rates used to set the value of trillions of dollars of investments, according to five dealers with knowledge of the practice.

Employees have been front-run[...] through trades before and during the [...] the current and former traders, who req[...] Dealers colluded with counterparts to b[...] people, who worked in the industry for a[...]

Enlarge image

A boy adjusts number tiles displaying the exchange rate on a currency exchange board at night in Bishkek, Kyrgyzstan. Photographer: Noriko Hayashi/Bloomberg

June 12 (Bloomberg) -- Bloomberg News' Liam Vaughn explains the process of currency trading and how traders are said to have rigged FX rates as Britain's market supervisor considers opening a probe into the practice. He speaks on Bloomberg Television's "On The Move."

The be[...] market[...] the value of funds and derivatives, the two traders said. The Financial Conduct Authority, Britain's markets supervisor, is considering opening a probe into potential manipulation of the rates, according to a person briefed on the matter.

"The FX market is like the Wild West," said James McGeehan, who spent 12 years at banks before co-founding Framingham, Massachusetts-based FX Transparency LLC, which advises companies on foreign-exchange trading, in 2009. "It's buyer beware."

The $4.7-trillion-a-day currency market, the biggest in the financial system, is one of the least regulated. The inherent conflict banks face between executing client orders and profiting from their own trades is exacerbated because most currency trading takes place away from exchanges.

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Nikkei 225 Futures Fall After BOJ Policy Statement

Why would the U.S. CFTC outsource the protection of U.S. taxpayers to anyone with such a poor record?

- In addition, foreign governments have a conflict of interest in enforcing effective rules on foreign banks: less or ineffective regulation will attract business & jobs to their country, with limited downside b/c U.S. pays the bill to bailout the global financial system
- That is why the CFTC was explicitly given the statutory mandate & duty to regulate these markets & market participants directly
  - To protect the U.S. financial system, U.S. economy & U.S. taxpayers
  - **If** substituted compliance is allowed, it must be robust in form, substance, enforcement & over time

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No More Delays: already 2 ½ years of CFTC consideration

- First CFTC meeting on cross border Jan. 2011
  - A year & a half of meetings, consideration, deliberation AND endless industry input
- Initial guidance proposed June 2012
  - Followed by yet more meetings, input, consideration, deliberation
- Additional guidance Dec. 2012, setting deadline of July 12, 2013, 7 months later
- After yet MORE input, latest draft circulated on May 16, 2 months before the deadline of July 12

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The American People have been waiting years already

- 3 years since the Dodd Frank financial reform law was passed
  - July 12, 2013 cross border deadline
  - July 21, 2010 Obama signed DFA
- 5+ years since the financial crisis
  - March 17, 2008 Bear Stearns failed
  - September 5, 2008 Fannie/Freddie receivership
  - September 15, 2008 Lehman Brothers failed
    - 2013 – this year – 5 year anniversary

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CFTC Must Finalize By July 12

- After more than 2 ½ years, it is time to finalize
- 4+ weeks left to work out any differences
  - Plenty of time
- SEC's recently proposed rule is inapplicable & weak
  - No basis for delay
- Objections based on speculation by foreign governments/industry no basis for delay
  - Will take years for them to put rules in place
  - Conflicts, **if any**, can be worked out later
- The time to protect the American people is NOW
  - Do not wait & do not start with lower standards
    - Can always change to address concerns; simply won't be able to increase

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Coming to a **U.S.** City Near You? **Not if** the CFTC Gets Cross Border Right

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Don’t Let This Happen Again

THE COST OF THE WALL STREET-CAUSED FINANCIAL COLLAPSE AND ONGOING ECONOMIC CRISIS IS MORE THAN $12.8 TRILLION

A Report From

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September 15, 2012

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