Commission de Surveillance du Secteur Financier

Macroprudential measures for GBP Liability Driven Investment Funds

Public Consultation Reply Form

Macroprudential measures for GBP Liability Driven Investment Funds

Responding to this paper

The Commission de Surveillance du Secteur Financier (hereafter 'CSSF') invites all relevant stakeholders to provide responses to the specific questions listed in the Consultation Paper on Macroprudential measures for GBP Liability Driven Investment Funds, published on the CSSF website.

Instructions

Please note that, to facilitate the analysis of the responses, you are requested to use this file to provide your response to the CSSF so as to allow us to process it properly. Therefore, CSSF will only be able to consider responses which follow the instructions described below:

- use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
- if you do not have a response to a question, do not delete it and leave the text "TYPE YOUR TEXT HERE".

Responses are most helpful:

- if they respond to the question stated;
- contain a clear rationale, including on any related costs and benefits; and
- describe any alternatives that CSSF should consider.

Naming protocol

In order to facilitate the handling of stakeholders responses please save your document using the following format:
CSSF_LDI Funds_ NAMEOFCOMPANY_ NAMEOFDOCUMENT

E.g. if the respondent were ABCD, the name of the reply form would be:
CSSF_LDI Funds_ ABCD_REPLYFORM or CSSF_LDI Funds_ ABCD_ANNEX1

Deadline

The deadline for receiving feedback is **18 January 2024.**
All contributions should be provided by filling in the present response form and sending it to the following address: opc_prud_risk@cssf.lu.

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Publication of responses

The CSSF intends to make feedback available on its website after the deadline for receiving responses has passed. Please do not include commercially sensitive material in your response, unless you consider it essential. If you do include such material, please highlight it clearly, so that reasonable steps may be taken to avoid publishing that material. This may involve publishing feedback with the sensitive material deleted and indicating the deletions.

While as indicated above, the CSSF will take reasonable steps to avoid publishing confidential or commercially sensitive material, the CSSF makes no guarantee that it will not publish any such information and accepts no liability whatsoever for the stakeholders' consultation responses that are subsequently published by the CSSF. Please be aware that you are making a submission on the basis that you consent to us publishing it in full.

General information about respondent

Name of the company / organisation	**abrdn**
Activity	Asset Management
Are you representing an association?	No

Introduction

Please make your introductory comments below, if any:

About abrdn

- abrdn is a global investment company that helps clients and customers plan, save and invest for the future. Our purpose is to enable our clients to be better investors.
- abrdn manages and administers £495.7bn of assets for clients (as at 30 June 2023).
- Our strategy is to deliver client-led growth. We are structured around three businesses – Investments, Adviser and Personal – focused on the changing needs of our clients.
- The capabilities in our Investments business are built on the strength of our insight – generated from wide-ranging research, worldwide investment expertise and local market knowledge.
- Our Adviser business provides financial planning solutions and technology for UK financial advisers, enabling them to create value for their businesses and their clients.
- Powered by the UK's second largest direct-to-consumer investment platform, interactive investor, our Personal business enables individuals in the UK to plan, save and invest in the way that works for them.

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List of questions

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QUESTION 1:	Do you consider that the proposed calibration of the minimum yield buffer is appropriate and the calculation of the actual yield buffer sufficiently clear?
ANSWER 1:	We consider the calibration at 300bps to be appropriate. The changes in interest rates illustrated in the paper could give the impression that the buffer is too conservative given it is a multiple of the worst cumulative move shown. However, these moves are using Close of Business levels and therefore underestimate the intra day volatility experienced prior to the BoE intervention. In practice, fund managers act upon intraday moves and therefore the cumulative move in excess of 2% for long-dated index-linked gilts prior to the BoE intervention is a better guide for setting a prudent buffer. The calculation of the actual yield buffer is clear. We consider the yield stress buffer to be the best metric of resilience as it captures both leverage and duration sensitivity. This metric has been used to manage and monitor abrdn’s leveraged LDI funds since their inception. As the minimum buffer is significantly bigger than pre-crisis, we could foresee a situation where LDI funds are managed very close to the limit in order to maintain a relatively high average leverage. However, leverage is not linear. For instance, a 100bps increase in yield from a starting leverage of 2x would increase leverage to 2.5x, but to 5x if the starting leverage is 3x. With a focus on minimum yield buffers, this acceleration effect tends to be underestimated. In order to avoid herd mentality, we consider the buffer prior to a recapitalisation being required to be nearly as important as the minimum yield buffer.
QUESTION 2:	Would you see merit in setting a minimum speed for the transformation into eligible assets (in days)? What would you consider the right minimum number of days, considering the settlement period for posting collateral to maintain leverage (repurchase agreements and/or derivatives)?
ANSWER 2:	We agree there is merit in setting a minimum speed. We would advise a maximum settlement period of T+2 to be aligned with collateral settlement.
QUESTION 3:	Do you agree with the proposed definition of LDI funds? In particular, do you consider that the definition is sufficiently clear and specific (i.e. only covering LDI funds)?
ANSWER 3:	We propose the following amended definition: "Any fund whose investment objective is determined with reference to matching the interest rate and/or inflation sensitivity of the assets to a pre-defined set of liabilities."

QUESTION 4:	Do you agree that LDI funds should not be allowed to consider for the yield buffer calculation any assets that are not their balance sheet? If not, please elaborate. In this case, what safeguards should in your view be considered?
ANSWER 4:	We agree that assets external to the fund should not be considered. It would be impossible to track except if counterparties have ultimate recourse to the underlying investors rather than the fund. Further, the manager cannot make an assessement of the liquidity and volatility of external assets where they have no direct control of those assets. This means they should not be required to determine how much of a risk mitigation these assets provide against the yield buffer.
QUESTION 5:	Do you consider that the mechanism driving the buffer usability is appropriate and sufficiently clear?
ANSWER 5:	Yes, we believe the methodology is suitable.
QUESTION 6:	What potential unintended consequences do you see from the proposed measures, and how could these be mitigated?
ANSWER 6:	Please refer to the second part of our response to Question 1.
QUESTION 7:	Do you have any other comment on the proposal?
ANSWER 7:	We believe that a key factor that contributed to the LDI crisis was the high degree of concentration of providers in the LDI market, with the bulk of LDI strategies managed by 3 participants. It was not the initial volume of net gilts sales that triggered the sharp rise in yields, but the expectation that a much larger amount would need to be sold. The prospect of having to make good these transactions was what ultimately triggered the spiral. As highlighted by the consultation document, there is a "high concentration of the LDI fund sector as the top three AIF managers account for 90% of the number of LDI funds". The market would benefit from diversification of LDI managers, limiting herd mentality and the ability for market participants to front-run the anticipated dynamics of a concentrated market. For instance, a maximum holding concentration per asset manager per strategy could be considered. Alternatively, asset managers identified as a source of material systemic risk should have additional responsibilities in relation to funds' pricing/liquidity requirements and perhaps a bigger risk buffer to deal with the market impact of their trading activity. This is the case in the banking sector, where more onerous requirements are placed on banks deemed systemically important.

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