
AFME Consultation Response

HM Treasury, Short Selling Regulation: Consultation on Sovereign Debt and Credit Default Swaps

7th August 2023

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the Short Selling Regulation Consultation on Sovereign Debt and Credit Default Swaps.

AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

AFME is registered on the EU Transparency Register, registration number 65110063986-76.

AFME members welcome measures intended to streamline the efficiency of the UK SSR. However, we would welcome further detail on the scope of the FCA's proposed emergency intervention powers, particularly in the scenarios deemed 'exceptional circumstances'.

In relation to the [Government's response to the Short Selling Regulation Review](#), we look forward to further consultation on the use of the market maker exemption and exempt share arrangements.

Consultation Questions

1. Do you agree with the analysis of the current SSR requirements set out in Paragraphs 2.5-2.10 (including our view on the impact on liquidity and settlement?)

Yes, we agree with the analysis set out in paragraphs 2.5-2.10.

Do you agree with the proposal set out in paragraphs 2.13-2.15? Please provide details to support your view, including any views on benefits and risks associated with the proposal.

Sovereign Debt

We observe that uncovered short selling in the sovereign bond market typically does not increase settlement risk. Short positions are generally well covered for settlement because of a highly liquid repo market in sovereign bonds. On this basis, we agree with the Government's proposal to remove requirements under Article 13 of the SSR.

Sovereign CDS

We welcome the Government's proposals to remove the restrictions on uncovered sovereign CDS. As stated in our [previous response](#) to the Government's Call for Evidence on the UK SSR, we believe that the objectives of greater liquidity and lowered borrowing costs in the sovereign CDS market can only be meaningfully achieved by removing these restrictions.

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We consider that removing the restrictions on CDS will enable more firms to participate in the market and in having CDS protection, there is potential for reduced volatility in stressed periods. There is no requirement to cover positions T+1, in the way that there is for gilts, and associated counterparty and settlement risks are managed by margin requirements on the derivative. This different market structure means that removing the restrictions on CDS could be beneficial to liquidity, particularly in stressed periods.

Emergency Intervention Measures

We observe that as per paragraph 2.15, the Government proposes to retain sovereign debt and sovereign CDS within the scope of the FCA's emergency intervention measures, which AFME members agree with. Members also note that the newly enacted Financial Services and Markets Act 2023 ('FSMA 2023') accords significant power to the FCA in repealing and replacing retained EU law, including the SSR regime¹. While we welcome the FCA's pragmatic approach to adopting emergency intervention measures with respect to short-selling, market participants would benefit from greater clarity on the scope of these powers.

We would like to request clarification on the scope of the FCA emergency intervention measures, specifically under Articles 18, 19, 20, 21 and 23 of the SSR. In our view, emergency measures such as short-selling bans have a detrimental impact on market liquidity and must only be enacted as a last-resort measure.

In reviewing the framework for the FCA's emergency powers under the SSR regime, we encourage the Government to consider the following:

- Providing further clarification about the information that the FCA can request or require to be disclosed and the timelines within which firms will be expected to provide this information.
- Should the FCA decide to issue a short selling ban in the case of market distress, we also recommend that they do so in a timely manner and that they provide the necessary clarity to the market on the scope of the ban.
- We would also welcome further clarity on the meaning of 'exceptional circumstances' as it relates to the FCA's emergency measures.
- Additionally, we would recommend that the approach used for long-term bans are also incorporated in the short-term bans' usage. Noting that we have provided evidence² which suggests that bans do not work and ideally should not be applied, we have previously recommend strengthening the safeguards that are currently in place for short-term bans. For example, the FCA could be required to confirm that a short term short-selling ban (Art 23 SSR) does not have a detrimental effect on the efficiency of financial markets which is disproportionate to its benefits. Whilst we anticipate that this assessment and a level of cost benefit analysis would already form part of the FCA's internal processes, the transparency of the confirmation would provide helpful clarity. The strengthening of the safeguards for the short-term ban in this way would be similar to part of the safeguard that currently applies to the long-term ban (Art 20(1) SSR).

Finally, we propose that any further changes to the regime governing the emergency powers of the FCA under the modified SSR regime should be subject to further industry consultation and engagement.

¹https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1168648/Building_a_Smarter_Financial_Services_Regulatory_Framework_for_the_UK_Plan_for_delivery.pdf - at paragraph 1.1, page 6

² https://www.world-exchanges.org/storage/app/media/short_selling.pdf

2. Do you have any further views on the matters set out in the consultation?

We have no further comments.

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