

MEMO# 32464

May 15, 2020

Update on SEC COVID-19 Market Monitoring Group Initiatives

[32464]

May 15, 2020 TO: ICI Members
Investment Company Directors
ICI Global Members SUBJECTS: Fund Governance
Operations
Portfolio Oversight
Risk Oversight
Systemic Risk RE: Update on SEC COVID-19 Market Monitoring Group Initiatives

On May 13, 2020, SEC Chairman Jay Clayton and Chief Economist S.P. Kothari issued a statement (“Statement”) to update investors, other market participants, and the public generally on the work of the SEC’s COVID-19 Market Monitoring Group (the “MMG”).[\[1\]](#) The SEC formed the MMG as a senior-level, cross-divisional team to study the effects of COVID-19 on markets, issuers, and investors.

The Statement provides insight into how extensively the SEC is engaging with domestic and foreign financial regulators and other public sector officials both in general and in identifying and responding to the effects of COVID-19.[\[2\]](#) It describes two separate initiatives that are underway to: (1) identify interconnections across key segments of the financial markets; and (2) analyze the risks and effects of investment strategies that include mechanistic portfolio management rules, guidelines, or restrictions.[\[3\]](#)

Interconnectedness Initiative

According to the Statement, the principal objective of the interconnectedness initiative is “to identify, analyze and clarify significant channels of risk exposure and risk transfer in our domestic and global financial system with an eye toward identifying areas of vulnerability and stability.” With a general focus on capital markets instruments and flows and their interaction with the broader financial system, the MMG is examining interconnections between credit origination, risk transmission, and investment and risk exposure, among other things. The MMG is seeking “to identify circumstances where shifts in risk assessment in one area may amplify risk-based price movements and capital flows in other areas.”

To be most effective in what otherwise could be a “massive and time-consuming undertaking,” the MMG is working with OFR, FSB and others to scope and sequence this

work. The MMG intends to examine select portions of domestic and global financial markets and identify which market participants, activities, and linkages act as the originators, transmitters, amplifiers, absorbers, and ultimate owners of risk. The SEC expects this work to facilitate further domestic and international engagement on “system risk and financial sector vulnerabilities” over the longer term.

Mechanistic Portfolio Management Initiative

In the mechanistic portfolio management initiative, the MMG will explore performance benchmarks and other rating-oriented portfolio guidelines that use credit ratings, downgrades, or other third-party metrics to trigger portfolio rebalancings, asset sales, or capital charges. The MMG will review whether, in the context of the effects of COVID-19 on credit markets, hypothetical risks associated with these activities are present and, if so, should be addressed. For example, the MMG seeks to understand whether there is a potential for “pro-cyclical” activity in the credit markets resulting from widespread mechanistic responses to credit downgrades.

The Statement indicates that as part of this initiative the Group is consulting with “a wide array of experts and stakeholders with diverse perspectives,” including investment advisers that manage mutual funds. The MMG anticipates briefing and working with regulatory colleagues, including the FSB, IOSCO, and FSOC, on this initiative.

Frances M. Stadler
Associate General Counsel & Corporate Secretary

Rachel H. Graham
Associate General Counsel

Bridget Farrell
Assistant General Counsel

endnotes

[1] See COVID-19 Market Monitoring Group – Update and Current Efforts (May 13, 2020), *available at*

<https://www.sec.gov/news/public-statement/statement-clayton-kothari-covid-19-2020-05-13>.

[2] The Statement discusses the MMG’s engagement with other US financial regulators and other authorities, including the Financial Stability Oversight Council (FSOC), the President’s Working Group on Financial Markets (PWG), and various government agencies represented on those bodies. It indicates that the SEC has been called upon to provide capital markets expertise to other regulators, including on Federal Reserve Board facilities and other market developments. The MMG also is working with foreign financial authorities and contributing to the work streams of multilateral organizations, such as the Financial Stability Board (FSB) and International Organization of Securities Commissions (IOSCO), regarding the impact of COVID-19 on markets.

[3] The Statement indicates that each of these initiatives “will support (as well as be

informed by) similar efforts being undertaken by the FSB, IOSCO and other organizations” and that the MMG will be working with the Office of Financial Research (OFR) on these matters.

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.