Leverage in Non-Bank Financial Intermediation: Consultation report

Response to Consultation

Institute of Economic and Financial Policy (IEFP)

Recommendation 1

1. **Is the description of the financial stability risks from leverage in NBFI accurate and comprehensive? Are there additional vulnerabilities or risk dimensions related to NBFI leverage that authorities should consider for monitoring purposes?**

   The IEFP finds the FSB's description and detailing of the various risks to the financial system concerning NBFI leverage to be comprehensive and accurate. We believe that there's sufficient theoretical and historical evidence to support the necessity for action regarding the risks that were identified and described as problematic.

   However, one major concern we believe the FSB should dedicate more effort towards is the increasing correlation amongst the portfolios of NBFIs. It has long been known that common ownership of various positions, and significant overlap between trades in general, pose severe risks to the financial system, even during an otherwise healthy economy. A recent prominent instance of this was during the temporary financial turmoil in August 2007, and the impact highly correlated hedge fund portfolios had on credit and equity markets when any participants faced financial pressure.

   We suggest that FSB recommend measures to disincentivize excessively correlated portfolios and ensure increased resilience in such portfolios. While this is expounded on in question 7, we recommend creating a committee to conduct quarterly evaluations of market conditions and trends and adjust margin, haircut, and other requirements accordingly. Specifically, they would increase borrowing and leveraging standards for asset classes with significant recent inflows and high long/short interest in other highly correlated assets. If followed, this recommendation would ensure a combination of quantitative and qualitative analysis to determine how to minimize instability within trades and the NBFIs involved in them.

   Furthermore, we would like to bring to the FSB a few proposed standards, rules, or regulations that the IEFP believes ought to be implemented only with significant care and deliberation, lest they contribute to increased instability and issues.

   The most prominent would be regulations or standards that call for increased transparency and for greater public access to financial conditions. While transparency is a critical component of free and democratic markets and can lead to higher degrees of accountability, it must be considered that public misunderstanding or confusion about public information

often leads to the very financial issues attempting to be prevented, such as the infamous stories of bank runs. The FSB should thus be deliberate when proposing increased financial transparency regarding positions and trades of NBFIs, and consider the impacts releasing such information might have.

A secondary concern is regarding the proposal for increased sharing of data between countries, and for countries to act together to ensure the sufficient enforcement of regulations and standards without regulatory arbitrage. Specifically, in order to ensure joint action that can't be capitalized on by other less-regulatory countries, we recommend clear guidelines and expectations to be stated in advance, and for the adoption of regulations to be deliberate.

2. **What are the most effective risk metrics that should be considered by authorities to identify and monitor financial stability risks arising from NBFI leverage?**

3. **What are the most effective metrics for the monitoring of financial stability risks resulting from:**

   (i) specific market activities, such as trading and investing in repos and derivatives

   The IEFP finds the most effective metrics to be gross and net leverage for measuring leverage against net capital. For derivatives, this should particularly account for both on and off balance sheet exposures. Additionally, the frequency of margin calls and high margin-to-exposure ratios in derivatives can be utilized to monitor general stability. For repo markets, monitoring haircuts applied to collateral gives insights into risk exposure between leverage providers and market participants. A combination of the following metrics can be utilized to monitor and piece together a general image of financial stability risks.

   (ii) specific types of entities, such as hedge funds, other leveraged investment funds, insurance companies and pension funds

   Metrics for monitoring hedge funds should include: leverage ratios, both net and gross, which capture the extent of exposure relative to the fund base. Derivative usage and off balance sheet exposure to monitor hidden leverage. Regarding insurance companies, we recommend the usage of asset/liability metrics for monitoring duration and liquidity mismatches between assets and liabilities, with general usage of investment concentration and portfolio leverage.

   (iii) concentration and crowded trading strategies

   The use of market and entry-level concentration ratios (HHI index) can quantify exposure across individual entities or a wider market, revealing systemic risk across the market. Margin utilization ratios can also be employed to find the likelihood of risks and margin defaults across the market.

Recommendation 3

4. **What types of publicly disclosed information (e.g. transaction volumes, outstanding amounts, aggregated regulatory data) are useful for market participants to enhance their liquidity or counterparty credit risk management? Are there trade-offs in publicly disclosing such information and, if so, what would be the most important elements to consider? What is the appropriate publication frequency and level of aggregation of publicly disclosed information?**

As stated in the response to question 1, transparency is undoubtedly an extremely important factor for both democratic markets and to ensure effective and targeted regulation. Indeed, there has been much historical precedent for increased transparency in markets increasing market efficiency and participation, while decreasing potential fraud and collusion. However, when determining whether to increase market transparency and access to information, the FSB must take into account the potential market impacts of the release of such information and the difficulties associated with collecting such information.

As has been already stated, while increased transparency and publicly disclosed information can lead to a more well-informed public, it can also cause the opposite of Alan Greenspan's irrational exuberance, namely, irrational gloom. Merely the perception of potential instability within the financial system can give rise to a self-fulfilling prophecy, as jittery participants might seek to exit positions and cause a pre-emptive and unnecessary market decline. Thus, while regulators should most certainly have access to relevant market information to accurately gauge the state of markets, that same information shouldn't necessarily be made publicly available.

However, market participants would certainly benefit from the publishing of data regarding liquidity, transaction volume, and net financial and synthetic leverage within the system

When it comes to the frequency of collecting and publishing data, regulators should strive to expend as few resources as possible when doing so while still gaining all that they need to make informed decisions. Given current "norms" or "standards" regarding the frequency of NBFIs providing or disclosing information, it seems reasonable to continue in that stead, with quarterly filings.

Recommendation 5

5. **Do Recommendations 4 and 5 sufficiently capture measures that would be used to address the scope of non-bank financial entities under consideration in this report? In what ways may the policy measures proposed in the consultation report need to be adjusted to account for different types of non-bank financial entities?**

   The IEFP broadly agrees with the ability of the measures discussed by the FSB to capture and address the vast majority of NBFIs and the leverage employed by them. As will be discussed in the answer to question 20, we believe that the only distinction to be made is based on the risk profiles of different kinds of NBFIs, and thus the degree to which they should be regulated.

6. **In what circumstances can activity-based measures, such as (i) minimum haircuts in securities financing transactions, including government bond repos, (ii) enhanced margin requirements between non-bank financial entities and their derivatives counterparties, or (iii) central clearing, be effective in addressing financial stability risks related to NBFI leverage in core financial markets, including government bond markets? To what extent can these three types of policy measures complement each other?**

   The IEFP agrees that the activity-based measures mentioned in the report can be and are effective at addressing financial stability risk and that all should be used effectively to mitigate risk and instability within the financial system.

Regarding minimum haircuts, the largest advantage of such a measure is its ability to mitigate the impact of artificially inflated asset valuations during times of high speculation. By effectively valuing the asset at less than its "true", ie. market, value, and minimum haircuts ensure that lenders and creditors are protected against at least some erosion in the market price of the asset. Thus, haircuts help slow down the cycle of cheap credit giving way to increased asset prices and speculation, which in turn fuels more cheap credit, and so on. However, their principal disadvantage is their static and fixed nature, which only provides limited protection to a certain degree.

Conversely, margin requirements, both initial and variation, are most useful during times of market change and volatility, as mark-to-market margin requirements ensure minimized counterparty risk. As a whole, margin requirements have been essential throughout the derivatives and other volatile markets, and in ensuring that even dramatic changes in market values don't result in debilitating losses. However, through margin calls, such requirements can also lead to the rapid destabilization and decline of markets, as borrowers sell off liquid and other assets to maintain their margin requirements

To this degree, the IEFP feels that CCPs can serve as the best solutions to ensure overall minimum stability and minimize the potentially negative impacts of leverage within NBFIs. By effectively eliminating counterparty risk within the largest financial markets, and barring the most extreme movements and events, CCPs ensure the financial system can operate as effectively as possible. Furthermore, their large reserves of liquid and cash assets ensure that even in the case of certain parties being unable to fulfill their contractual obligations, their counterparty is able to continue operating and receive their payments. Additionally, during times of low liquidity and credit crunches, CCPs continue to aid the connection of borrowers and lenders, such as for repo markets, allowing for the financial system to not get excessively gummed up.

The IEFP also appreciates the fact that the incentives of CCPs—namely market stability, liquidity, and effective use of capital markets—line up extremely well with those of regulators. As such, due to their own profit motive, CCPs can allow a proverbial "devolution" within the field of regulation. Finally, their ability to access and effectively utilize large amounts of data much quicker than federal bodies means that they can internally adapt their own changes in margin and haircut requirements, allowing federal regulations to act only as a "line of last defense", in the case of extraordinary negligence.

7. **Are there benefits to dynamic approaches to minimum margin and haircut requirements, e.g. where the requirements change based on changes in concentration or system-wide leverage? If so, what types of indicators capturing concentration or system-wide leverage should the requirements be linked to?**

The IEFP finds that dynamic and adaptive management of minimum margin and haircut requirements will be essential in limiting the frequency and severity of leverage-induced market downturns while maintaining the stability of capital markets and supporting asset growth.

To ensure flexibility and commensurate standards and requirements, financial regulators should strive to use the following factors to identify the degree of potentially dangerous system-wide leverage and thus reasonable minimum haircut and margin requirements.

One: the aggregate/net leverage of NBFIs across various markets, which can be calculated from different sources at local and national levels, such as CCPs, margin debt statistics from

agencies such as FINRA, and the aggregate of NBFIs' gross leverage ratios. The use of net global and market-specific leverage figures would likely be the most important indicator, allowing regulators to gauge the risk of current and future potential exposure and leverage and make effective decisions moving forward.

Two: volatility indicators, such as the VIX for equities, CDS premiums, credit spreads, and the MOVE Index for debt and bonds, and recent historical volatility for asset classes in general. Leverage, particularly synthetic, can both be caused by and cause increased volatility: increased volatility often causes margin calls and higher premiums, and those same margin requirements and market fear fuel more liquidations and volatility.

Three: position overlap indicators, such as Factor Exposure Clustering and the Herfindahl-Hirschman Index to broadly assess the degree of correlated returns amongst NBFIs. Such indicators can mathematically identify portfolio overlap and overexposure that has long scourged financial markets without a detailed breakdown of positions and asset correlations and can be used by regulators to adjust trade-specific margin and haircut requirements to ensure minimum strain on markets.

Hence, such indicators will effectively identify any necessary changes in minimum haircut and margin requirements, allowing for growth and effective investment allocation while broadly preventing excess leverage in the system. To practically implement such indicators, we recommend creating a quantitative program and/or a committee/board that'll analyze quarterly data to determine any changes in borrowing and leveraging standards in markets, specific securities, or specific trades; with regulatory experts or machine learning and other algorithms determining optimal changes in requirements in markets given changes in indicators and conditions.

Importantly, we stress that dynamic changes in margin requirements should not be applied to any currently open positions, contracts, or borrowing NBFIs are engaged in but only to any future trades or actions. Should this principle be violated, any quarterly change margin requirements might lead to a flood of forced liquidations, causing unimaginable harm to the financial system.

8. Are there any potential unintended consequences from activity-based measures beyond those identified in the consultation report?

While the consultation report provided successfully addresses the majority of concerns or unintended consequences that might come about from activity-based measures, there are a few issues we believe need to be addressed at a higher level.

The first issue is regarding the potential for additional requirements to inhibit effective asset allocation, reducing funding in capital markets, and thus potentially stifling the funding of innovation and valuable enterprises. While already-established corporations often can and do innovate and lead to technical and/or technological advances, smaller startups or other companies that are funded by debt (directly or not) often play critical roles in such areas.

Yet, activity-based measures that decrease leverage by NBFIs can damage the ability of such companies to receive funding and operate most effectively. Due to the fact that the majority of investment and funding startups receive come from NBFIs in various forms, the ability of NBFIs to increase their leverage and allocate more of their assets toward productive investments is of key significance to advancing innovation.

Thus, if higher margin or haircut requirements are imposed upon such NBFIs, they'll have to hold more liquid and non-volatile assets, resulting in less money going to investment-worthy innovative enterprises as a whole, and a semi credit crunch for such companies. As such, the FSB ought to consider the impact of any activity-based measures on private capital markets and the potential reduction in investments in innovative technology and ideas.

Another potential consequence of activity-based measures is increased consolidation and decreased competition amongst NBFIs. As an evident consequence of the relationship between risk and return in a portfolio, measures that intend to decrease potential risk within the financial system and its members will inevitably impact the maximum possible return earned by such participants. However, the impact of such decreases will disproportionately be felt by smaller NBFIs with fewer AUM.

Operating, administrative, and fixed costs make up a disproportionately higher percentage of assets in NBFIs with less capital, and thus the same percentage decrease in investment returns will result in a lower net return for investors in smaller NBFIs. As a consequence, smaller or newer funds might experience increased withdrawals of capital to be invested in larger funds, decreasing competition in the space, which will likely carry the long-term consequence of decreased returns and increased risks for investors.

This can be seen in the decline in the number of hedge funds, certain kinds of investment banks, and other NBFIs that followed the implementation of regulations such as Basel III, all while net AUM stayed the same or grew, indicating increased consolidation. The FSB should thus take these two potential unintended consequences into account when developing proposed regulations or standards for leverage.

9. For non-centrally cleared securities financing transactions, including government bond repos, what are the merits of margin requirements compared to minimum haircuts?

As per its typically accepted definition, and the one presented within the paper, minimum haircuts are static and unchanging, and are simply one-time transactions that accompany any "financing transactions". The primary downside to the use of such a static measure rather than a dynamic and adapting one, such as margin requirements, is the inability of such a measure to be prepared for all potential market conditions, and thus work in all cases.

As stated when responding to question 7, the FSB and other regulatory bodies must ensure standards and requirements are not excessive enough to depress capital or derivative markets during less risky or speculative times. As such, unless regulatory bodies observe or have some reason to believe in a lack of risk-aversion in the market, and dynamically adjust minimum haircut and margin requirements—again, as proposed in the response to question 7—haircuts would generally be expected to be relatively moderate.

Thus, during a sudden deterioration in market conditions, ie. an increase in volatility and risk, that occurs during a time of low minimum haircuts and margin requirements, static minimum haircuts represent disproportionately small percentages of the collateral value given the hypothetical volatility. Therefore, they would have done little to decrease leverage in the system beforehand and would have done nothing to protect lenders or creditors. Yet this problem wouldn't exist for margin requirements, as daily marking to market would ensure that, in the absence of unprecedented price changes, creditors would have enough of a liquidity buffer to recoup their loan, if need be. Thus, margin rather than minimum haircut

requirements would allow for cheap access to credit during risk-averse and nonvolatile times, while affording much more protection during times of market stress.

Furthermore, when specifically addressing OTC trades without central clearing, counterparty risk is an obvious factor that must be considered. As stated above, in the case of sudden and extreme market volatility compared to the percentage haircut, the initial haircut might easily evaporate, leaving the lender unprotected. Conversely, variation margin requirements would ensure that any unfavorable price movements would be balanced out by the borrower by the end of the day, dramatically decreasing the possibility of complete default, and thus counterparty risk.

As such, it can be seen that margin requirements have various advantages compared to minimum haircut requirements, and will provide room for growth and upside during healthy markets while protecting market participants in the case of adverse price changes.

10. In what circumstances can entity-based measures, such as (i) direct and (ii) indirect leverage limits be effective in addressing financial stability risks related to NBFI leverage in core financial markets?

The IEFP finds that entity-based measures, such as direct and indirect leverage limits, can be highly effective in mitigating financial stability risks when applied under appropriate circumstances. Direct leverage limits, which impose explicit restrictions on an institution's overall exposure, are most effective when there is a high degree of data transparency and clarity in business models.

In environments where the financial exposures are well-documented and relatively straightforward, these limits provide a clear boundary that helps prevent excessive risk accumulation. This is especially important in core financial markets, where a few large players dominate and where the failure of one entity could potentially trigger market-wide systemic issues.

In contrast, indirect leverage limits, implemented through mechanisms like risk-weighted asset requirements are particularly valuable in settings where financial activities are complex, with significant off-balance sheet or synthetic exposures that might not be fully captured by direct measures alone.

11. Are there ways to design and calibrate entity-based measures to increase their risk sensitivity and/or their effectiveness in addressing financial stability risks from NBFI leverage?

The use of dynamic calibration frameworks that adjust leverage thresholds in response to real-time market conditions and forward-looking indicators, such as volatility, liquidity, and haircuts. Additionally, enhancing the granularity of these measures by disaggregating different types of leverage—such as gross, net, and synthetic—and integrating collateral quality and margin adequacy metrics can provide a more precise assessment of an entity's risk exposure.

Tailoring these measures to reflect the unique business models and risk profiles of various non-bank financial institutions further ensures that the regulatory framework remains both proportionate and adaptive, thereby bolstering its overall effectiveness in mitigating systemic risks. Therefore, the IEFP recommends allowing measures to become more sensitive in times of financial risk, allowing for maximum utility in high-risk scenarios while otherwise having minimal impact on financial activities.

12. **Are there any potential unintended consequences from entity-based measures beyond those identified in the consultation report?**

Beyond the unintended consequences noted in the consultation report—such as the potential reduction in liquidity provision by key market participants and the risk of risk-shifting through reallocation across activities—additional risks may emerge. For instance, overly rigid entity-based limits might compel complex, multi-strategy firms to restructure in order to circumvent these constraints, thereby obscuring true risk exposures and inadvertently fostering regulatory arbitrage as entities shift activities to less regulated or opaque channels.

Such shifts could distort competitive dynamics and diminish market efficiency by undermining the sophisticated risk management practices that allow firms to align leverage with specific risk profiles. Moreover, if entities migrate to jurisdictions with more lenient constraints, the global effectiveness of these measures could be compromised, ultimately increasing systemic vulnerability. These broader potential consequences highlight the need for careful calibration and ongoing review of entity-based measures to ensure that they do not inadvertently exacerbate financial instability.

13. **To what extent can activity-based and entity-based measures complement each other? What are the main considerations around using these two types of measures in combination?**

Activity-based measures, which target specific market activities through mechanisms like margin and clearing requirements, and entity-based measures, which impose overall leverage or concentration limits on individual institutions, can complement each other by addressing different facets of financial stability risks. When used in combination, activity-based measures help to constrain risk-taking behaviors across all market participants, ensuring that immediate liquidity and counterparty risks are managed, while entity-based measures provide a tailored approach that directly limits the aggregate exposures of particular non-bank financial entities.

The main considerations for their joint application include ensuring that the measures are carefully calibrated and designed to avoid excessive burdens or unintended market distortions, such as incentivizing risk migration to less regulated sectors or triggering liquidity constraints and that they are harmonized across jurisdictions to mitigate regulatory arbitrage. In essence, when these measures are dynamically aligned and mutually reinforcing, they offer a more robust framework for mitigating both systemic vulnerabilities and entity-specific risks.

Recommendation 6

14. **How could counterparty credit risk management requirements for leverage providers be enhanced to be more effective in addressing financial stability risks from NBFI leverage in core financial markets, such as government bond repo markets? In what circumstances can they be most effective?**

There are two primary means through which counterparty credit risk management requirements could be meaningfully enhanced to reinforce financial markets and reduce the frequency and degree of future market problems.

The first involves improved collateral or margin requirements that ensure that risk and volatility can be effectively handled during tumultuous times. As stated throughout this

paper, we find that CCPs and dynamic margin/haircut requirements can be most effective at allowing for growth in capital markets and asset values, while still preventing excesses and dangerously high leverage.

The second major method, specifically for CCPs and other central intermediaries, involves the enhancement of current CCP data collection and utilization methods. Without delving too deep into specifics, making use of financial and other data to identify the potential for risk, volatility, or instability within markets and systems can allow central intermediaries to take preliminary measures to diminish such possibilities.

Recommendation 7

15. **Would a minimum set of disclosures to be provided by leverage users to leverage providers be beneficial in improving counterparty credit risk management and reducing financial stability risks from NBFI leverage, including concentration risks? If so, which types of information and what level of granularity should (and should not) be included in this minimum set and why?**

    A minimum set of disclosures from leverage users to their providers can play a pivotal role in enhancing counterparty credit risk management and mitigating financial stability risks, particularly those arising from concentrated NBFI leverage. Such disclosures should ideally include key metrics such as aggregate exposure levels, detailed information on the concentration and size of leveraged positions, collateral composition and quality, liquidity profiles, and trends in transaction volumes. The granularity should be sufficient to allow leverage providers to accurately assess risk without revealing overly sensitive or proprietary details that could compromise competitive positions. Striking this balance is essential to ensure that the data supports effective risk management while protecting strategic business information

16. **What are the main impediments that leverage users face in sharing additional or more granular data with their leverage providers? Is there a risk that a minimum recommended set of disclosures may lead leverage users to limit the information they share with their leverage providers to that minimum set?**

    Confidentiality concerns, technological constraints, and the varying regulatory requirements across jurisdictions can limit the extent and timeliness of detailed disclosures. Moreover, there is a real risk that a prescriptive minimum disclosure framework might incentivize firms to limit their reporting strictly to the mandated items, potentially curtailing the voluntary sharing of valuable supplementary information. This “minimum standard” effect could hinder comprehensive risk assessment if firms opt to share only the bare minimum required rather than a fuller picture of their risk exposures.

17. **Should such a minimum set of disclosures rely on harmonised data and metrics to ensure transparency and efficiency in the use of such information for risk management purposes? Do respondents agree that such a minimum set of disclosures should be based on the list of principles outlined in the consultation report? If not, which principles should be added, deleted or amended?**

    N/A

18. **Should leverage users be required or expected to provide enhanced disclosures (beyond that provided in normal market conditions) to their leverage providers during times of stress?**

    During periods of market stress, enhanced disclosures from leverage users can be particularly valuable. Requiring more detailed and frequent reporting in times of stress would allow leverage providers to gain real-time insights into rapidly changing exposures, liquidity conditions, and potential concentration risks. Such enhanced disclosures should include more granular data on large or rapidly shifting positions, updated liquidity metrics, and stress test outcomes, among other critical indicators. However, it is equally important that these requirements are carefully calibrated to avoid imposing excessive administrative burdens or triggering unintended market disruptions during volatile periods

19. **Should authorities design a minimum set of harmonised disclosures and guidelines on its application, or should they convene a cross-industry working group to do so? How do respondents believe such a standard should be incorporated into market practice? Through regulation, supervisory guidance, and/or via a Code of Conduct or similar approach?**

    With respect to the designer of regulatory and reporting standards, it seems most prudent to have the regulatory agencies themselves establish the requirements based on what information they might need for any analysis or assessments.

    Furthermore, it is evident that information and data regarding major market participants and regarding the markets as a whole are of utmost importance to regulators, particularly when incorporating several of the recommendations mentioned in this response. Additionally, if only provided to regulatory agents and the government, NBFIs won't face any unintended consequences or increased risks as a result of providing data.

    Thus, in order to ensure that regulatory bodies make the best possible decisions with the maximum information available, there ought to be strict regulations that ensure that NBFIs provide the data and disclosures needed. Nonetheless, it must be recognized that, be it to skirt disclosing requirements or prohibitions on activities, NBFIs can and do use a variety of legal, accounting, or other maneuvers to avoid such regulation. An extremely prominent example was the utilization of derivatives and other forms of synthetic leverage to skirt the strict margin requirements by Regulation T and other acts. Burdensome regulation that aims to identify and deal with every possible edge case or scenario would also likely fail to work, and would almost certainly have unforeseen consequences or negatively impact market efficiency or liquidity.

    With this in mind, the IEFP views most favorably the creation of internal departments or sub-agencies within regulatory agencies that have relatively broad powers for enforcing or preventing trading or disclosure activities. We specifically call for the expansion of the European Securities and Markets Authority (ESMA) model, with standard and harmonized rules, and the discretion to act as needed based on market conditions. Even when hampered by the lack of certain disclosure requirements and access to certain market data and information, the ESMA has been able to act effectively on numerous occasions to prevent potentially excessively unstable conditions. They've done so all while maintaining overall and long-term market liquidity and efficiency, as has been confirmed by multiple studies.

Thus, we envision a similar regulatory setup, with access to increased data and information, the ability to establish default harmonized standards, and the power to use such data to make dynamic changes in requirements and standards regarding NBFI leverage (ie. margin and minimum haircut requirements).

However, the intended objective of such an agency should not be to actively engage in discretionary behavior and regulation, but to instead only do so when prudent and necessary; rather, a significant advantage would be its ability to use its access to data and ability to change standards to take preemptive action to prevent market instability to the highest possible degree.

Recommendation 8

20. Are there areas where the principle of "same risk, same regulatory treatment" should be more consistently applied? Are there circumstances in which the principle should not apply or should not apply comprehensively?

The IEFP broadly recommends applying the principle of "same risk, same regulatory treatment", with the caveat that "risk" refers to both activity-based and entity-based risk. In general, we find that the most simple, cost-effective, and comprehensive method to regulate financial markets and behavior involves categorizing both potential trades or position types that involve leverage, as well as different kinds of NBFIs based on perceived risk.

When it comes to actually classifying NBFIs according to their risk, the IEFP would recommend utilizing disclosure filings combined with broad assumptions about the type of NBFI as a whole to effectively gain an understanding of the risk that might be posed to financial systems with various combinations of NBFIs and trades. However, due to the impracticability of performing a particularly thorough or advanced analysis, and the potential negative impacts of excessive requirements and maintaining such standards of liquidity and market efficiency, we recommend that the principle be broadly applied, with comprehensive analysis only being done in the case of extreme market conditions.