MEMORANDUM

TO:	File
FROM:	Division of Trading and Markets
RE:	Meeting with members of the Credit Roundtable and Fixed Income Forum
DATE:	February 10, 2012

On February 10, 2012, staff from the Division of Trading and Markets, Division of Investment Management, Division of Corporation Finance, and Division of Risk, Strategy, and Financial Innovation met with the following individuals: Matthew Abbott (Wellington Management Company, LLP); Robert Auwaerter (The Vanguard Group); Patrick Cassidy (Nationwide Investments); Chris Gootkind (Loomis, Sayles & Company, L.P.); David Knutson (Legal and General Investment Management); Mike Lillard (Prudential); Carolyn Perlmuth (Institutional Investor); John Rosenthal (Metropolitan Life Insurance Co.); Adam Rubinson (Dodge & Cox); Chérie Schaible (AIG Asset Management); and Louis Zahorak (CalPERS).

The purpose of the meeting was to discuss the proposed implementation of the Volcker Rule. The discussion primarily focused on the exemption to the prohibition on proprietary trading for market making-related activity.

Attachment

Volcker Rule Discussion on Proprietary Trading in the Bond Markets

2/10/12

Rule Objective: Avoid putting taxpayer money at risk to pay out depositors in the event of a bank failure due to "proprietary trading"

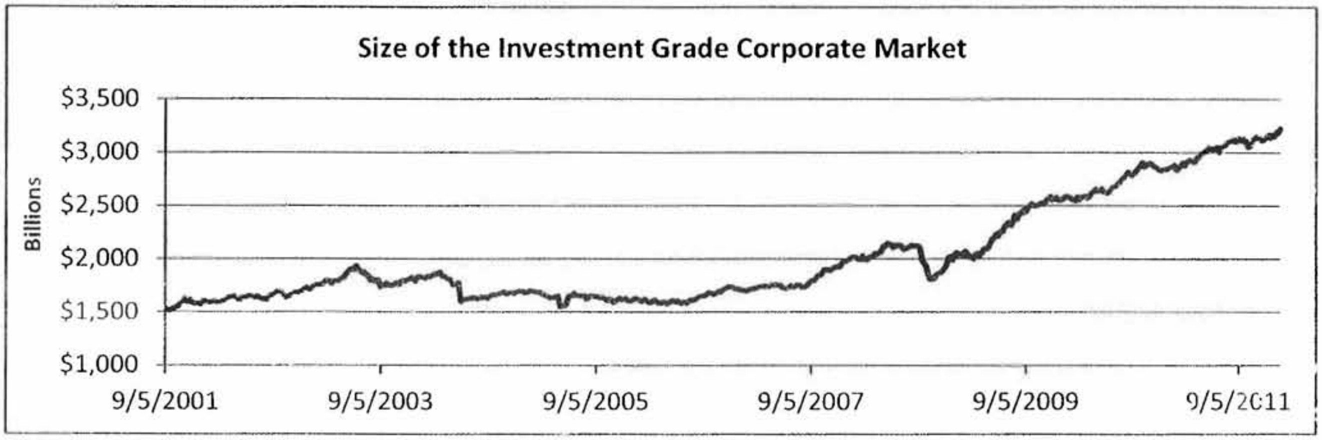
One Potential Approach:

1. Do not focus on a legalistic definition of a "proprietary trade", which is very hard to define in the bond markets where securities dealers have to hold bond inventories on their books due to the fragmented, over the counter nature of the market.
2. Instead, focus on broader measures of risk of the banks' security trading portfolio
3. Example below:

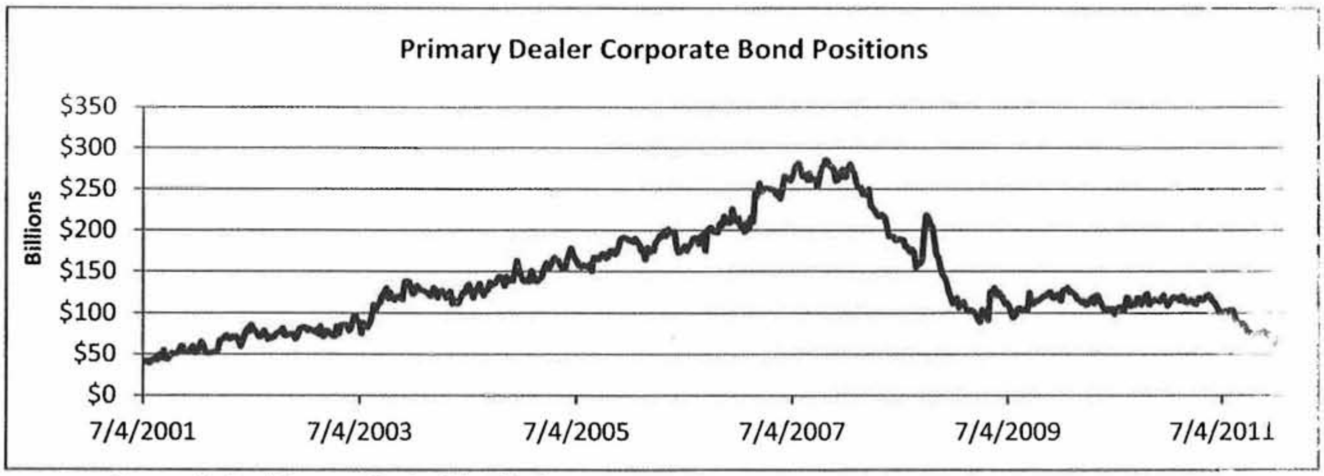
Aging Securities Inventory

1. A general principle of trading is that the longer you hold a trading position, the greater the potential for it to generate a loss
2. Trading firms with good risk management functions put each security held in inventory into time held buckets (such as 0-45 days, 46-90, 91-180, 181-365) and charge the trader a carrying cost that increases as the security moves into the longer dated buckets. This directly negatively impacts the profit and loss of the trader's trading book. This makes it more costly for a trader who is trying to "hide" a prop trade in his book.
3. Different types of securities have different carrying costs (the more illiquid the security, usually the higher the carrying charge)
4. Regulators could assess the bank's Aged Inventory Policy relative to other firms for the appropriate level of rigor.

Investment Grade Corporate Bond Liquidity



Source: Barclay's Capital Investment Grade Corporate Index



Source: Federal Reserve Bank of New York

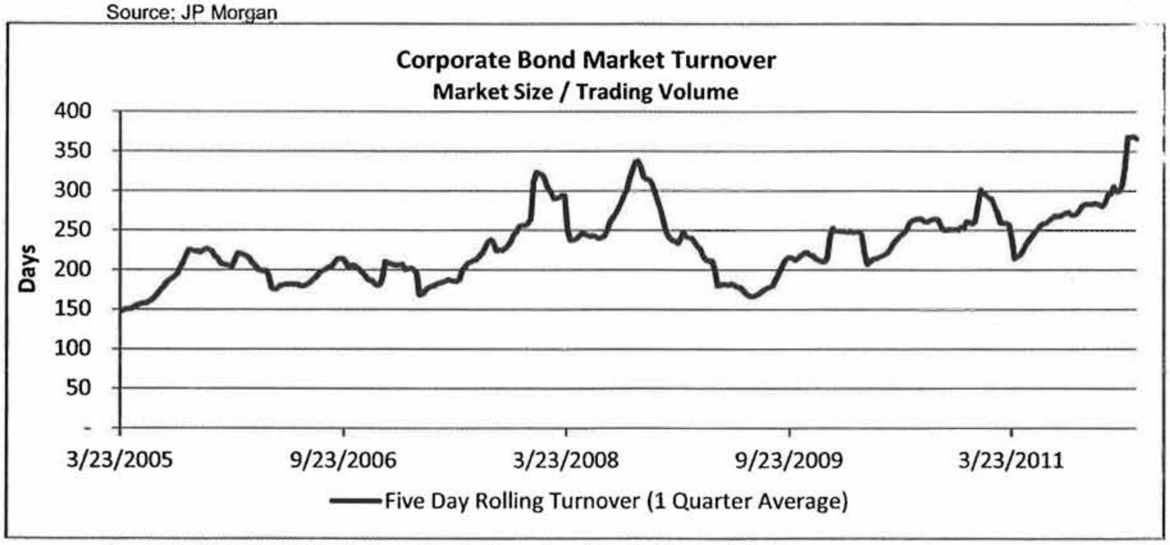
Source: Barclay's Capital Investment Grade Corporate Index & Federal Reserve Bank of New York

Investment Grade Corporate Bond Trading Volume

Source: FINRA TRACE

*Five Day Rolling Average

Source: JP Morgan



Source: FINRA TRACE & Barclay's Capital Investment Grade Corporate Index

Asset Class	Average Daily Trading Volume ($bn)	Amount Outstanding ($tn)	Turnover in Days
Equities	4,200	11	3
Treasuries	580	9.9	17
Investment Grade Bonds	11.8	3.2	270
HY Bonds	4.4	1.2	270

Source: JP Morgan

As of: November 2011