Managed Funds Association
The Voice of the Global Alternative Investment Industry
Washington, D.C. | New York | Brussels | London

May 8, 2023

Via Email
The Honorable Gary Gensler
Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Recent Market Events

Dear Chair Gensler,

Managed Funds Association[1] ("**MFA**") appreciates your statement reminding the public of the Securities and Exchange Commission's (the "**SEC**" or "**Commission**") focus on and dedication to identifying and prosecuting market misconduct.[2] We also appreciate the indication that the Commission remains committed to fair and efficient markets and is not currently contemplating any short sale ban.[3] Nevertheless, the regional banking crisis is prompting certain market participants and commentators to shift the focus away from the core challenges facing certain segments of the banking system by advocating for a short sale ban on select bank stocks. This is unwarranted and would cause greater harm to investors, markets, and the very issuers subject to those restrictions. We write to urge the Commission to refrain from imposing any short sale bans.

SEC data from 2008 and numerous academic studies show that short selling bans are harmful and are counterproductive to their purported end goals. Banning short selling will only increase market volatility, hurt price discovery, and delay a recovery in regional banks' prices. We wholeheartedly agree with the SEC's long-held view that short selling contributes to efficient and orderly markets.[4] As you know, the SEC implemented a short selling ban regarding certain financial institutions during the Great Financial

[1] Managed Funds Association ("**MFA**"), based in Washington, DC, New York, Brussels, and London, represents the global alternative asset management industry. MFA's mission is to advance the ability of alternative asset managers to raise capital, invest, and generate returns for their beneficiaries. MFA advocates on behalf of its membership and convenes stakeholders to address global regulatory, operational, and business issues. MFA has more than 170 member firms, including traditional hedge funds, credit funds, and crossover funds, that collectively manage nearly $2.2 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time.

[2] Statement on Current Market Events, Chair Gary Gensler (Mar. 12, 2023), https://www.sec.gov/news/statement/gensler-statement-current-market-events-050423.

[3] PoliticoPro Morning Money, May 5, 2023.

[4] Short Sales: Concept release; Request for comments, 64 Fed. Reg. 57996, 57997 (Oct. 28, 1999) ("Short selling provides the market with two important benefits: market liquidity and pricing efficiency"), https://www.govinfo.gov/content/pkg/FR-1999-10-28/pdf/99-27879.pdf.

Crisis. Upon review of this action, the SEC's own analysis led Former SEC Chair Christopher Cox to admit that the costs "outweigh[ed] the benefits."[5] The SEC staff found that the extreme negative returns in bank stocks were not the result of short selling, and that in fact, overall short sellers were contrarian traders with activity peaking during periods of positive returns.[6] A 2012 study conducted by the Federal Reserve of New York and supported Chair Cox found that bid-ask spreads increased 3.43 times for U.S. stocks that were subject to the ban, increasing trading costs for investors by $500 million during that two-week period.[7] In addition, it found that the ban did not prevent stock prices from continuing to fall. In fact, stock prices did not stabilize until the ban was lifted.

Further, a short-selling ban would have the unintended consequence of harming the banks themselves. Research of the 2008 ban by Choi, Getmansky and Tookes shows that banning short selling impaired the ability of banks to raise the capital needed to weather the storm.[8] Considering their findings, a short sale ban would impede the ability of banks to secure new capital, such as by issuing convertible bonds.[9]

Moreover, the SEC already has controls that protect against excessive market volatility. Post-financial crisis, the Commission adopted regulatory measures such as circuit breakers and the short sale uptick rule, which have proven effective in preventing panic selling and ensuring orderly markets.[10] We believe these tools, along with the SEC's ongoing efforts to monitor and penalize market manipulation and other abuses, should ensure investor confidence in the stability and integrity of our markets without resorting to blanket bans on short selling.

MFA supports the SEC's efforts in "identifying and prosecuting any form of misconduct that might threaten investors, capital formation, or the markets more broadly." Malfeasance has no place in well-functioning markets. Naked short selling and other such abusive practices are already illegal and should be investigated. Short selling as a practice, however, contributes to the health of the markets and should not be a scapegoat for issuers who experience stress.

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[5] Letter from Daniel Aromi & Cecilia Caglio, Office of Econ. Analysis, SEC, through James Overdahl, Chief Economist & Dir. of the Office of Econ. Analysis, SEC, to Christopher Cox, Chairman, SEC (Dec. 16, 2008), https://www.sec.gov/files/s70809-369.pdf.

[6] *Id.*

[7] Press Release, Federal Reserve Bank of New York, Short-Selling Bans Failed to Prevent U.S. Stock Price Declines (Aug. 10, 2012), https://www.newyorkfed.org/newsevents/news/research/2012/rp120810.

[8] Convertible Bond Arbitrageurs as Suppliers of Capital, Choi, Getmansky and Tookes (July 2009) (finding that convertible bond arbitrageurs are important suppliers of investment capital to issuers, and their inability to hedge their risks through shorting the underlying security led to a significant decline in the ability of issuers to raise capital.).*See also*, Alessandro Beber & Marco Pagano, *Short-Selling Bans Around the World: Evidence from the 2007–09 Crisis*, 68 J.Fin. 343 (Feb. 2013), https://www.eief.it/files/2013/01/pagano_beber_joff_2013.pdf.

[9] *Id.*

[10] SEC Investor Bulletin: New Stock-by-Stock Circuit Breakers, Aug. 1, 2011, https://www.sec.gov/oiea/investor-alerts-bulletins/investor-alerts-circuitbreakers; Press Release, Securities and Exchange Commission, SEC Approves Short Selling Restrictions (Feb. 24, 2010), https://www.sec.gov/news/press/2010/2010-26.htm.

MFA and our members are available to provide additional industry insight as the SEC and other regulators navigate the regional banking crisis. We support the SEC's work to promote the long-term stability and health of our financial markets, including the recognition that short selling is a net benefit to the strength of our economy.

We appreciate your attention to our concerns and look forward to further engagement on these pressing issues.

Sincerely,

/s/ Bryan Corbett

Bryan Corbett
President & CEO

cc: The Hon. Hester M. Peirce, Commissioner
The Hon. Caroline A. Crenshaw, Commissioner
The Hon. Mark T. Uyeda, Commissioner
The Hon. Jaime Lizarraga, Commissioner
Dr. Haoxiang Zhu, Director, Division of Trading and Markets
Dr. Jessica Wachter, Director, Division of Economic Research and Analysis