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FRBNY Email from Miknius re Notes from Various Calls and Meetings at Morgan Stanley

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To
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Subject
Notes from various calls/meetings at MS

Notes from meeting with Ken DeRegt, MS CRO. In some cases these comments are restating what was gathered in earlier meetings, though in some cases fresh points or figures are presented. At the end are a few additional points from another conversation with Tom Wipf who heads up secured financing for MS and Anita Rios, COO in MS's Treasury Dept.

Funding was priority one for him when the day started - all has gone above expectations. Europe rolled easily and no real problems in NY (fully funded and more so early - no triparty returns - cash in mortgage space 20% above normal and he assumes that is cash previously placed to Lehman). There were a few (5-6) requests for additional collateral. He understands this was a system-wide event and normal given the circumstances. They will continue to monitor these and alert us if they accelerate - they did not accelerate throughout the day today. They will use the PDCF for $4B across all asset classes - not for need but to test as agreed by other market participants.
His biggest issue is in operations and relates to ops at Lehman in two ways. He has a high level of concern and already raised these issues to senior SEC and FRB staff. Firstly, things are not moving well at all within LEH operationally - mostly in equities - it creates confusion in determining what MS's current exposure is to LEH - they feel exposure is going up during the day, but they don't want to be taking on much LEH risk. Secondly, they have clients with PB assets at LEH that are looking to move to MS. These clients are indicating that nothing is happening at LEH creating worry. In select cases MS will work with these clients to facilitate a sale/buy transaction to get the securities from LEH to MS, but MS is concerned about the potential for taking on LEH risk.
Market-wise, MS CDS spreads widened by 125-150 bps with very little trading going on. MS and GS shares are both down about 8% (meeting was at 1PM today) whereas MS shares were down more than GS earlier in the day. MS exp to moves in the market today was limited and it was generally right-way risk. He does not have any other specific counterparty concerns as of now though they are running stress tests on that front (AIG exposure was described as minimal) - only a few CPs raised concern about MS - mainly European banks and those have been worked out. He cited no issues with MS's ability to flatten its market risk positions in the wake of the LEH collapse.
Ken mentioned that they are being very alert to requests for cash that are "not normal". Noted one instance where a large PB client wanted to monetize a specific in-the-money derivative exposure - Ken and MS decided not to allow - told them to take all of their business away or none - don't cherry pick.

One last point from Ken - he is a proponent of the weekend LEH netting exercise that ultimately died out - he was disappointed it didn't come to fruition because currently it is left to be voluntary and it seems more could be done by everyone to spur the process forward.

From Tom Wipf...

Tom updated us on the status of funding for the TFP secured funding program. They lost $2B from JPM Inv Mgmt where they were told they were doing the same for all remaining IBs. He clarified that the $1.5B lost from State Street was in fact a request for higher grade collateral, not a complete pull away, where MS is left trying to find another lender to support the weaker collateral. Lastly, they anticipated going into the day and did, in fact, lose $2B of O/N funding from conduit sources. Pulling together all of these, they were able to find other sources so the net impact is a loss of $2-3B of TFP funding which will likely just be drawn from the liquidity pool (which was relatively high at $83B going into today).

Tom further indicated that for JPM in particular they suspect a call will be made from the CEO level to try to work out the issues. He felt the other names would likely be dealt with more at the line/desk level. Lastly he mentioned BlackRock and Franklin Templeton as names where calls may be needed to appease name concerns. For Franklin Templeton its because they just put MS on their internal watch list.

From Anita Rios...

Clarifying some details regarding the JPM collateral request as clearing agent for MS, Anita indicated that they were told from JPM that the request was made in part because it's a fairly new relationship (2yrs) and all required legal paperwork has still not been signed and put in place. We note that JPM apparently made similar collateral requests from other IBs using different rationales. Also, we are not clear as to whether MS is under the impression that the cash collateral would no longer be necessary once the legal paperwork was finalized.

Regarding the BoNY mention earlier, we learned that BoNY did not actually ask for cash collateral and MS has not placed any cash with them. They $4B figure mentioned earlier was an increase in the amount MS Credit Risk staff would permit to be left at BoNY during the normal course of business.

Finally we got some clarity around the various clearing agents MS uses globally. BoNY is their securities clearing agent in the US; JPM is their main securities clearing agent in Europe; HSBC is their largest securities clearing agent in Asia. BNP Paribas, DB and Commerz are used as securities clearing agents for a variety of niche markets throughout Europe while Std Chartered plays a smaller clearing role in Asia for MS. Citibank is their primary cash clearer for the parent company in the US.

Jeff & Angela