



Yale SCHOOL OF MANAGEMENT
Program on Financial Stability

EliScholar – A Digital Platform for Scholarly Publishing at Yale

YPFS Resource Library

4-30-2010

FCIC memo of staff interview with Mabel Yu, Vanguard Investments

Mabel Yu

Nathan Will

William Roberts

Bruce Mcwilllams

Ryan Bubb

<https://elischolar.library.yale.edu/ypfs-documents/5990>

This resource is brought to you for free and open access by the Yale Program on Financial Stability and [EliScholar](#), a digital platform for scholarly publishing provided by Yale University Library. For more information, please contact ypfs@yale.edu.

MEMORANDUM FOR THE RECORD

Event: Interview with Mabel Yu, Vanguard Investments

Type of Event: Phone interview

Date of Event: Friday, April 30, 2010; 3:00pm

Team Leader: Brad Bondi

Location: 1717 Pennsylvania Avenue, Suite 800, Washington, DC; Small conference room

Participants - Non-Commission:

- Nathan Will, Associate Counsel, Vanguard
- Mabel Yu, Credit Analyst, Vanguard
- Bill Roberts, Head of Taxable Analysts, Vanguard

Participants - Commission:

- Bruce McWilliams
- Ryan Bubb

MFR Prepared by: Karen Dubas

Date of MFR: April 30, 2010

Summary of the Interview or Submission:

This is a paraphrasing of the interview dialogue and is not a transcript and should not be quoted except where clearly indicated as such.

MCWILLIAMS: [Talks about creation of FCIC]. I'd like to talk about Ms. Yu's call with Mary Elizabeth Brennan that was memorialized in the internal Moody's memo that was posted by the House Oversight Committee. What were your responsibilities at the time?

YU: My formal title was junior credit analyst. I was responsible for structured finance, CMBS, ABS, ABCP, and a little RMBS.

MCWILLIAMS: How long were you with Vanguard at the time?

YU: About 7-8 years.

MCWILLIAMS: You've been there for 10-11 years now?

YU: I started at Vanguard in 1996 or 1997. I was trained as an auditor, and then I got an MBA and my CPA. Then I was a controller and did financial analysis. I did project planning for the website at Vanguard and I did strategic planning before I moved to Fixed Income and Structured Finance.

Did you speak to Ms. Brennan?

YU: Yes.

MCWILLIAMS: How did you know to call her?

YU: She approached me and requested that I talk to her.

MCWILLIAMS: Did your supervisor know that the call would take place?

YU: At that time, no.

Moody's had been trying to get my opinion for awhile, and I was really, really busy. They had made repeated calls so finally I agreed to talk to them. It was a customer relationship call. They wanted to see whether we were happy with their service.

MCWILLIAMS: Did Vanguard pay Moody's?

ROBERTS: Vanguard paid Moody's and other rating agencies for research and ratings. Our largest expense outside of compensation is the fee we pay rating agencies. The model is described as issuer-paid because the largest portion of the rating agencies' revenues comes from the issuers. It cost us several hundred thousand a year for research.

MCWILLIAMS: Were you Mabel's supervisor at the time?

ROBERTS: No, Chris Alwine was. He was my predecessor and still works at Vanguard.

YU: I'm an industrial analyst now.

MCWILLIAMS: You make a reference to a caller in the memo. Do you know who that is?

YU: No, it was from an industry conference call. That was the other person who was frustrated. I was listening to the call; I wasn't giving any of my opinions during the call, but other people did.

MCWILLIAMS: Vanguard bought less and less of the asset class and stopped buying entirely in 2006?

YU: Vanguard did not buy much of subprime because at a very high level, we're not a company that takes very high risks. Subprime was new, and we looked at it very cautiously. We looked at it carefully and recognized that there was a lot of risk in it. We didn't buy any, and then we bought a little and then less and less.

We look at investments and the risk that we take and the price that we take—the spread—and ask whether the price that we paid is enough to compensate us for the risk that we take? Our independent analysis was that it was better for us not to buy more of this asset.

ROBERTS: We were very skeptical of the asset class then and we were fortunate that we didn't buy large positions in it. I'm not sure that we stopped buying it by 2006; I'd want to verify that to make sure it's correct.

MCWILLIAMS: Are all the comments on here correct for your memory?

YU: I think that's how I felt, that was my personal opinion. But opinion is not fact.

MCWILLIAMS: Do you remember who you talked to at Moody's?

YU: I spoke to many different analysts, because I typically had several deals on my desk each day. I talked to many, many of them. It's not unusual to talk to several analysts each day. I also talked to other sources -- other rating agencies.

English is my second language. I may have used the word 'one analyst,' but I meant that I was talking about analysts in general.

MCWILLIAMS:

She wants to "have a dialogue" with the agencies and feels strongly that an Aaa in sub-prime isn't the same as an Aaa in credit cards. In her role at Vanguard, Yu is overwhelmed by the number of new issues and secondary issues in the market today and wishes she could rely more on rating agency opinions. Yu feels that Aaa "doesn't mean that we're protected anymore."

Can you think of specific transaction where AAA was different?

YU: It was not specific; it was a general trend. If I had only noticed it in one or two transactions, I would not have taken the time to express my opinion.

MCWILLIAMS:

She explains her analysis of new CMBS deals: "When I look at a deal, I have to do a deep dive on loan quality, loan-by-loan, and then I have to take a haircut. All this analysis takes time."

YU: Vanguard had strict standards so when I look at the sell-side and the rating agencies, I pick up a more conservative approach.

MCWILLIAMS:

Yu then commented a bit about frustrations she's faced in analyzing CMBS transactions. she noted that in the reports, rating agencies are clear about their stress levels but are not clear about why they are stressing at those levels. She feels that "risks are not laid out" and that when talking to analysts she needs to be very specific in her questions and "know exactly what to ask to uncover risk."

Did you feel that Moody's should have done that?

YU: They did it, but it was in a different way. There's an academic debate all the time about how to stress the risks, how much risk tolerance to have, what kinds of assumptions should be made.

WILL: The SEC has made the determination that loan-by-loan transparency is necessary. They've just passed a rule with Regulation AB for loan-by-loan data.

MCWILLIAMS:

She felt that sometimes her questions were too specific and she was frustrated when analysts would reply "I can't answer that or I'd be giving you 'preferential treatment.'" Yu commented, "If that's their problem, that makes me uncomfortable. Rating agencies aren't helping me to make the right decisions. They are giving just enough information to make a decision but not enough to be fully informed. They are not helping out."

You talk about the analysts. You'd be specific in your questions and they'd be unresponsive?

YU: I talk to many analysts every day. I think that's part of the challenge. I think there's a new SEC rule that requires more transparency and a minimum of five days to review the deal.

ROBERTS: Another part of the new rule proposal is a minimum of 5 days between when the data is available and when the deal is closed. Before this rule, you might have an hour to review the deal.

BUBB: How do Moody's, S&P, and Fitch compare in their analysis of mortgage-related structured finance products, or structured products in general?

YU: When I discussed this with Ms. Brennan, I had only been in structured finance for about 18 months, and I was certainly not an expert. Only 10% of my time was RMBS; most of my time was CMBS, ABS, and ABCP. Vanguard invested a little in CDO, but only very early on.

My main job at Vanguard is to safeguard our assets and protect our clients. The rating agencies were only one of my reference points for making an independent evaluation. My role was not to evaluate them. I look at them as a data point.

I felt like we might need to stress the ratings more to protect our clients, and I'd do my independent analysis. I can never justify an investment recommendation based on the rating agencies. That's why I've declined all requests to participate in industry conferences because I feel like I'm not an expert; my focus is only Vanguard. I've been gone from my former position

for almost 15 months now, so I've been removed from structured finance for quite awhile and don't keep up with it anymore.

BUBB: In your remarks from 2007, it's apparent that you used the rating agencies as one data point. You concluded that the ratings of structured products were less meaningful. Did you feel like that was more true of Moody's than S&P?

YU: I really didn't think about it like that. Moody's called me. It was a courtesy that I participated in that call. I was really busy and I was looking at deals all of the time. It wasn't so much that I had a big opinion that I expressed to the world.

BUBB: Does anyone else at Vanguard have views about the ratings for structured finance?

ROBERTS: I didn't have a role in that from 2004-2008. There are 25 senior analysts at Vanguard, and if you asked for their view of rating agencies, you'd get very different opinions. The rating agencies were stronger in certain sectors.

If you really are interested in views about the rating agencies, I can put you in touch with our structured finance analyst. He wasn't at Vanguard during that time period, but he was involved in the industry at the time. (Bob Behal)