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Before Greensill Failed, It Relied on Wall Street

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LONDON -- The founder of Greensill Capital spoke frequently about disrupting big banks. But before the financial startup collapsed this month, it relied on the apparatus of Wall Street to fuel its expansion.

Greensill's closest Wall Street relationship was with Credit Suisse Group AG, which provided it financing through $10 billion of investment funds. But a clutch of other big players -- including Citigroup Inc., Morgan Stanley, Ernst & Young, and Moody's Investors Service -- played key roles in Greensill's rise.

Citigroup expanded its business with Greensill despite repeated warnings internally not to do so because of reputational issues, according to people familiar with the Citigroup-Greensill relationship. The big U.S. bank operated a trust that processed payments for Greensill's borrowers, forwarding money on to investors in the Credit Suisse funds. Citigroup also worked on a failed last-ditch attempt to raise fresh capital for the startup.

Greensill was founded in 2011 by former Morgan Stanley and Citigroup banker Lex Greensill. The firm specialized in supply chain finance, a form of short-term corporate lending.

Greensill planned to outmaneuver big banks that dominate the industry with better **technology** and by offering the service to more clients. Many of Greensill's clients were blue-chip companies, though it also made other, riskier loans that were longer-term or for borrowers that were more precarious.

Greensill filed for bankruptcy earlier this month after it lost credit insurance that was crucial to its business. Credit Suisse suspended the investment funds. Greensill's bank in Germany is under investigation by authorities into its accounting for loans to a major client.

The startup's business model required complex financial engineering. It made supply-chain loans to companies, then packaged them up into notes, selling those on to investors, which served as off-balance-sheet financing for Greensill.

Citigroup operated a trust for Greensill, according to a Greensill marketing document and the people familiar with the Greensill-Citigroup relationship.

Such trusts are commonly used on Wall Street to handle the details of moving money among financial entities. Yet employees on Citigroup's trade finance team raised concerns in conversations and emails multiple times over the past five years about doing business with Greensill, according to the people.

Some of the warnings, which centered on Greensill's business practices, were made to senior managers who oversaw treasury and trade, trusts and banking coverage, one of the people said.

In 2019, employees brought their concerns to the bank's business practices committee, which assesses conflicts of interest and other reputational risks to the bank, one of the people said.

The business practices committee's response couldn't be determined, though Citigroup expanded its business with Greensill in 2020 when it helped the company hunt for fresh capital, The Wall Street Journal has reported.

A Citigroup spokesperson declined to comment.

Greensill also leaned on Morgan Stanley, which for several years acted as an intermediary between Greensill and the investors in the notes. These included funds at Credit Suisse and Swiss asset manager GAM Holding AG, according to people familiar with the funds and the Greensill marketing document reviewed by the Journal.

Morgan Stanley provided the funds with information about the notes, including pricing and duration of the underlying loans, and placed the notes with the funds for a fee, the people said.

Morgan Stanley also helped Greensill's biggest client in 2019, when GAM shut a fund that had been an important source of financing for Greensill. Some of the assets in the GAM fund were tied to businesses owned by U.K. steel magnate Sanjeev Gupta.

Morgan Stanley used a special-purpose vehicle to repackage about GBP 220 million, equivalent to $300 million, of Greensill-arranged bonds related to Mr. Gupta's businesses held in the GAM funds. Morgan Stanley then sold them to its clients, according to some of the people familiar with the funds.

Big Four accounting firm EY had a close-up look at Greensill's business. In 2019, EY performed investing due diligence on Greensill for SoftBank Group Corp.'s Vision Fund, Greensill's biggest outside investor, according to a SoftBank investment memo reviewed by the Journal.

EY told the Japanese investor it faced several risks, including that Greensill relied heavily on a handful of clients for most of its revenue, and that access to trade credit insurance was a constraint on Greensill's business.

EY said in the memo that it expected Greensill to diversify its pool of clients and that insurance would become less important as Greensill established a successful record. Those expectations didn't come to pass. Greensill collapsed into insolvency after a major credit insurance provider said it would stop providing new coverage.

By February this year, EY had become wary of working with Greensill because of the possible reputational hit, according to people familiar with the matter.

Credit ratings company Moody's rated three multibillion-dollar funds at GAM and Credit Suisse that invested in securities created by Greensill. The funds were given the third-highest rating on Moody's scale for bond ratings, which indicates that assets are generally considered "upper-medium credit quality."

The ratings were important to Greensill because they made it possible for a broader pool of investors to buy into the funds. The Moody's analysts noted that sometimes the assets were concentrated in just a handful of Greensill clients.

It wasn't until March, however, until after the funds were suspended, that Moody's downgraded the Credit Suisse-Greensill funds and put the GAM-Greensill fund on review for downgrade.

A Moody's spokesperson declined to comment.

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Year-End Review & Outlook: Markets & Finance (A Special Report) --- New Army of Individual Investors Arrives, Flexes Its Muscle

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The online brokerage industry might be hard pressed to outdo the record-breaking year it experienced in 2020, but for now, few are betting against it.

Individual investors opened more than 10 million new brokerage accounts in 2020, JMP Securities estimates, a record. Interest isn't fading, either: App downloads for brokerage firms, while lower than earlier in the year, remain resilient, with the Robinhood Markets Inc. app expected to reach 500,000 downloads in December alone, data provided by the investment bank shows. Website traffic for well-entrenched brokerages, including TD Ameritrade Holding Corp. and E*Trade Financial Corp., continues to increase as well.

"You have this incredibly engaged customer," said Devin Ryan, senior research analyst at JMP Securities. "It appears that the end-customer is actually logging into their account more than they were at the beginning of the pandemic."

The year will be known as the time when individual investors dove into financial markets and doubled down, even in the midst of a global pandemic, strapping in for a roller-coaster ride that sent stocks plummeting -- and then skyrocketing -- in record time.

Driving the interest was a combination of factors that started with an industrywide shift to commission-free trading in 2019 but swelled as market volatility grew. As the coronavirus rolled across the U.S., millions of new investors found themselves stuck at home, some with extra time on their hands to learn about the markets. Others, unable to bet on sports or visit casinos, found the stock market's outsize swings presented the perfect outlet to make bets.

In some cases, those wagers became a part of investing sensations, owing to the countless online forums where traders gathered to swap ideas. Similar to the online chat rooms that surrounded the late-1990s dot-com bubble, social-media sites such as Facebook, TikTok and the messaging platform Discord became hubs to talk up trades, sometimes helping send shares of companies on a wild ride.

Some investors, including prominent figures such as Dave Portnoy, used the spaces to tout gains and lament losses. Mr. Portnoy, founder of the popular digital media company Barstool Sports Inc., began streaming trades to his followers, who now approach two million, on Twitter. "Stocks only go up," Mr. Portnoy would proclaim, reiterating the phrase that had become popular on internet messaging forums.

For a while, as stocks zoomed higher, the mantra seemed to hold up. Three months after markets bottomed in March, shares of companies from Moderna Inc. to Tesla Inc. to Peloton Interactive Inc. had all jumped 130% or more. Individual investors piled into those stocks while snatching up shares of smaller companies, too. Perhaps most notoriously, they sent shares of companies including Hertz Global Holdings Inc. and Chesapeake Energy Corp. soaring, despite the financial crises the companies faced. The companies, both of which filed for bankruptcy protection, were ultimately delisted from the New York Stock Exchange.

On peak trading days in 2020, individual traders are estimated to have accounted for nearly 25% of U.S. trading activity, Citadel Securities estimates. Overall, their share of total trading volume doubled to an average of 20% from 10% in 2019, Citadel said.

Analysts say individual traders likely make their biggest impact in driving share prices of smaller or less-popular companies, though they remain robust buyers of the same megacap **technology** companies and other stocks that institutional investors own. Webull Financial LLC said Tesla and Apple Inc. were the most popular stocks on its trading platform in 2020. TD Ameritrade pointed to Amazon.com Inc. and PayPal Holdings Inc. as among the most heavily purchased companies during November.

Retail platforms -- Robinhood, in particular -- have become the subject of increasing scrutiny. In December, Massachusetts regulators filed a complaint against the company, saying it failed to protect users' assets and encouraged inexperienced customers to make risky trades. Robinhood, which disputes the allegations, says it has added safeguards for options trading, which is generally considered to be a more complicated -- and at times riskier -- strategy. It also maintains that only 13% of users who traded in any given month in 2020 made an options bet.

"We see evidence that many of our customers are classic 'buy and hold' investors," said Vlad Tenev, Robinhood's CEO.

Robinhood in May said that the number of users of its platform had reached more than 13 million. Analysts believe that number is now higher. The app popularized free trading, thanks, in part, to its mobile-first, easy-to-use platform and the promise of free stocks when signing up or referring friends to join.

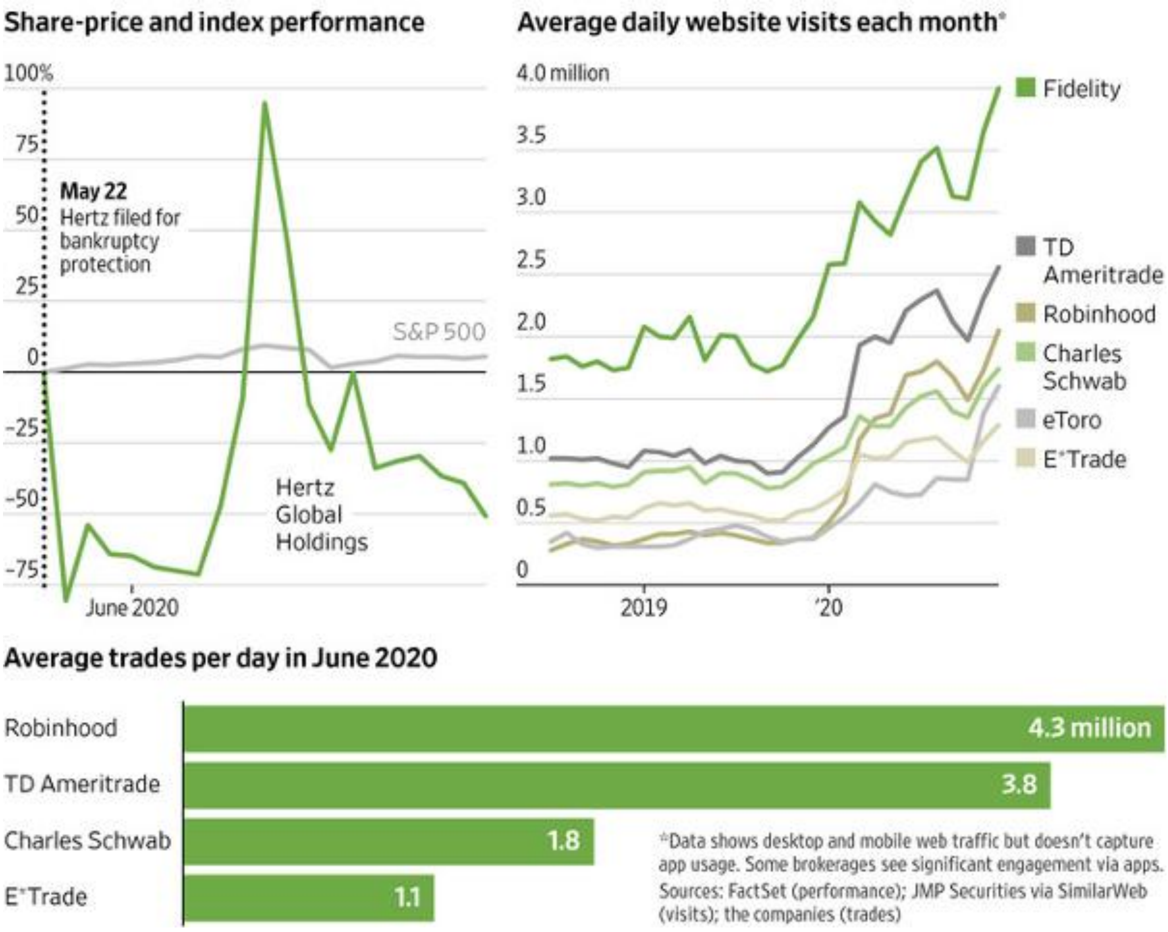
Despite the attention on the riskier trades that investors executed, studies have found individual investors performed well in 2020. A June note from Goldman Sachs Group Inc. analysts found that a basket of the stocks most popular among individual investors had outperformed hedge-fund and mutual-fund favorites -- as well as the broader market -- since the March lows, due to individual traders' quicker embrace of value stocks. Other analyses from researchers similarly found that individual investors didn't significantly panic when markets tumbled in 2020, which rewarded them when stocks began rising.

Although a debate about the risks and rewards that online brokerages enable is likely to continue, few analysts or financial advisers argue that enticing people to begin investing earlier is a bad thing. Studies have repeatedly shown that investing early can lead to bigger gains later in life. The recent introduction by online brokerages of tools such as fractional investing -- or the ability to buy just a portion of a share -- has made trading big-name companies more accessible, too.

The past year "created a new generation of investors that are seeking more," Mr. Ryan of JMP Securities said. "They want tools, they want education, they want to do more."

Mr. Ryan noted that significant growth opportunities for brokerages are possible, especially if they continue to expand their product offerings. The ability to capture investors' wallets while they are young, and then work to become the main financial relationship in their lives via trading, banking, wealth management and other services offers some firms significant potential, he said.

"If you think about the customer today, I think there's a lot of attention on their small accounts," he said. "But these are small accounts today that in 20 years could be very large accounts."



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