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A dynamic year for APAC securities finance markets

The easing of the short selling ban in South Korea, strong lending demand in Taiwan, the BHP unification event in Australia, and a reliable stream of income from Japan, all contributed to a standout performance for APAC in terms of revenue generated per lendable assets.

Revenue generated from securities lending globally reached US$10.9 billion in 2021, according to S&P Global data, the highest since the financial crisis. This was powered by a resurgence in APAC equity finance revenue, which totalled over US$2 billion and fell just short of the region's best year in 2018. The year-on-year increase of 33 per cent for APAC was the highest change for any region globally.

Taiwanese SBL growth was one of the key stories across the street in 2021. The industry has seen record trading balances as the market continues to grow in both onshore and offshore trading. Hong Kong and Malaysia also performed strongly, with Malaysia's Top Glove Corporation the top revenue-generating security over the year according to S&P Global.

Elsewhere, short selling was reintroduced in South Korea in May, limited to constituents of the KOSPI 200 and KOPSI 150 indices, and this has resulted in strong demand for selected stocks. Contributors noted that the sheer size of the Japanese market once again meant it was one of the region's top revenue generating markets, despite being heavily GC-driven with limited noteworthy specials activity during the year.

Geopolitics had a heavy impact on borrower demand for loan securities in Hong Kong and China. The waxing and waning of trade tensions between the US and China, which hit their apogee in the final period of the Trump presidency, have continued to impact securities finance strategies. In early 2021, the focus was on US sanctions on investments in Chinese companies deemed to have links with the military.

By mid-year, attention was shifting to regulatory tightening across certain sectors, including China's technology, private education, and property segments. Liquidity concerns surrounding Chinese property group Evergrande were, by late 2021, generating contagion fears and driving strong sector lending demand. Northern Trust notes that China's clampdown created conditions which enabled marketwide short conviction not seen since before the COVID-19 pandemic. The Hang Seng Index finished down 15 per cent for the year, justifying the downside conviction.

In September, five leading regional securities lending associations came together to form the Global Alliance of Securities Lending Associations (GASLA), an alliance that seeks to deliver closer collaboration on global priorities for the industry.

Industry-wide efforts to drive standardisation of documentation are a prime example of this regional cooperation. With this in mind, the Pan Asia Securities Lending Association (PASLA) has entered into a new legal services arrangement with the International Securities Lending Association (ISLA) regarding the development of the Global Master Securities Lending Agreement (GMSLA) suite of documents, which became effective in January 2022.

With ESG considerations increasingly important to the future of securities lending, PASLA and the Risk Management Association (RMA) combined their expertise to launch the Global Framework for ESG and Securities Lending (GFESL) in May.

More broadly, work continues to support nascent and developing securities lending markets in APAC. For example, in the Philippines industry working groups are focusing on changes to short selling regulations to enable use of GMSLA and offshore collateral. For Indonesia, an industry working group has assisted Bank Indonesia with its plans for introducing securities lending for Indonesian bonds.

In China, industry associations have been communicating with Chinese regulators and exchanges on the utilisation of the stock borrowing facility via the Qualified Foreign Investor (QFI) channel. Complexities around the operating model have meant that meaningful participation for offshore lenders is still relatively limited. Industry groups continue to work with the financial authorities in China and Hong Kong to encourage lending opportunities connected with QFI (formerly QFII), Stock Connect and synthetic channels.

Bob Currie
Group Editor, Securities Finance Times

Inside this handbook

Inside this handbook

Asia strong as global securities finance revenues dip

Global securities finance revenues fell by 15 per cent YoY during January to US$836 million, with global equity financing revenues recording their lowest monthly figure since February 2021, according to recently published data from IHS Markit, now part of S&P Global.

This decline can be attributed particularly to tighter equity spreads for EMEA and the Americas.

Rising borrower demand evidenced last year for exchanged-traded products, corporate bonds and American Depositary Receipts (ADR) has reversed, with ADR revenues dropping 58 per cent YoY. Americas equity revenues for January fell 44 per cent YoY to US$269 million and EMEA equity revenues contracted by 29 per cent to US$80 million.

The APAC region continues to deliver the highest average fees globally at 99 per cent, with Malaysia, South Korea and Taiwan heading the region with average fee rates of 4.79 per cent, 2.48 per cent and 2.47 per cent respectively.

APAC equity finance revenues rose 37 per cent YoY during January to US$175 million — with Taiwan (US$49 million, up 178 per cent YoY) and South Korea (US$35 million, up 324 per cent YoY) delivering the largest contribution.

Australia also saw its equity finance revenues rise, up 160 per cent YoY to US$21 million.

Revenue from US equities finance fell to US$244 million in January, a decline of 46 per cent YoY from January 2021 when the markets were benefiting from the tailwind provided by new special purpose acquisition company (SPAC) deals and trading related to the retail short squeeze. Average fees improved slightly for Americas equity month-on-month, up 12 per cent for January, but were down 50 per cent YoY.

Citi establishes clearing and settlement facility for Beijing Stock Exchange

Citi China has established links with the China Securities Depository and Clearing Corporation Beijing Branch to provide clearing and settlement services for the new Beijing Stock Exchange (BSE) and National Equities Exchange and Quotation Company (NEEQ).

In doing so, Citi says that it has become one of the first international banks to develop clearing and settlement links for the new stock exchange and to become fully established to support trading for Qualified Foreign Institutional Investors (QFIIs).

China announced plans in September 2021 to launch a new stock exchange in Beijing, creating the third stock exchange on the mainland alongside the Shanghai Stock Exchange and the Shenzen Stock Exchange.

The BSE is fully owned by NEEQ, a Beijing-based execution venue providing over-the-counter trading in smaller companies, typically before they list on other exchanges.

The BSE will concentrate on innovation-oriented small and mid-sized enterprises (SMEs), strengthening the capital-raising channels available to these mid-tier companies. It is expected that many companies currently trading on NEEQ will migrate onto the BSE.

GCEX sets up office in Kuala Lumpur

GCEX, a Financial Conduct Authority-regulated digital brokerage, has opened an office in Kuala Lumpur, with investment from True Global Ventures, the venture capital firm.

The expansion into Malaysia is part of a wider effort to enhance GCEX's service for its growing client base in Asia.

The first team member in operations has already joined the firm, with four additional hires planned by May 2022.

Founded in 2018, GCEX provides a digital asset and FX platform for liquidity providers, lending counterparties and digital custody asset institutions.

GCEX is headquartered in London, with offices in Scotland and Denmark. Its office in Denmark opened in September 2021.

Lars Holst, founder and CEO of GCEX, says: "Expanding our global footprint into Asia is a significant development for GCEX and a key milestone in our growth strategy. We selected Kuala Lumpur as our Asia hub as we believe it is one of the fintech capitals of Asia, with a strong pool of talent for us to access as we grow the business.

He adds: "The investment we received from True Global Ventures (TGV4 Plus) is helping to fuel our expansion, enabling us to capitalise on the growing demand we are seeing for our modular end-to-end plug and play trading platform for digital assets and foreign exchange."

Standard Chartered HongKong to acquire RBC Investor Services Hong Kong

Standard Chartered Bank Hong Kong (SCBHK) is to acquire RBC Investor Services Trust Hong Kong Limited, subject to regulatory approval.

The acquisition aims to enhance SCBHK's securities services capabilities and client base as part of a wider effort to grow its custodian and fund servicing business.

SCBHK also aims to expand into the Mandatory Provident Fund (MPF) and Occupational Retirement Schemes Ordinance (ORSO) schemes trusteeship business in Hong Kong.

RBC Investor Services Trust Hong Kong is an indirect subsidiary of of Royal Bank of Canada and an approved trustee authorised by the MPF Schemes Authority.

It provides a full suite of services, including trustee, fund administration, custody and transfer agency services to MPF and ORSO schemes, as well as other Hong Kong and offshore investment funds.

Commenting on the acquisition, Mary Huen, CEO of Hong Kong, Standard Chartered, says: "Hong Kong is a key market to Standard Chartered. We remain highly confident in the outlook as Hong Kong continues to grow as an international financial centre. The acquisition demonstrates our commitment to investing in growth areas, enhancing our client offering and supporting the development of the retirement planning industry."

Francis Jackson, CEO of investor services, RBC Investor & Treasury Services, comments: "Our strategy is to focus on North America and Europe – our key markets of growth. We thank our colleagues and clients in Hong Kong for their partnership, and remain committed to supporting each of them during the transfer."

ISLA adopts PASLA annexes to the GMSLA

The International Securities Lending Association (ISLA) and the Pan Asia Securities Lending Association (PASLA) entered into a legal services arrangement for GMSLA documentation.

The arrangement regarding the Global Master Securities Lending Agreement (GMSLA) will facilitate the development of future annexes and addendums identified as requisites for securities lending activity in Asia Pacific markets.

This step toward digitisation of industry documentation was announced last month with the objective of enabling firms to

Korean repo volumes surge in 2021

The Korean Securities Depository (KSD), a triparty repo agent, has announced a dramatic surge in repo trading volumes in 2021.

Volumes increased by 5.3 per cent YoY to US$19.6 trillion in 2021, according to KSD's data on opening settlement.

The new record high represents a 75 per cent increase from US$11.2 trillion in 2017.

The daily average trading volume rose by 18.8 per cent YoY to US$106.0 billion in 2021, which is a 107 per cent increase on US$51.1 billion daily ATV in 2017.

By the end of 2021, the repos traded among institutions in Korea were 12-fold larger than call loans.

Overnight repos make up the largest share at 68.2 per cent, US$72.5 billion of the entire trading volume, while the rest is composed of longer-term transactions. The growth was largely driven by the excess liquidity during the COVID-19 pandemic and the sizable purchase and sale of government securities under open market operations.

ISLA and PASLA enter into new legal services agreement

The International Securities Lending Association (ISLA) and the Pan Asia Securities Lending Association (PASLA) have announced they will step into a new legal services arrangement for GMSLA documentation.

The agreement, which became effective in January, allows further collaboration between these associations and the development of the Global Master Securities Lending Agreement (GMSLA) documentation suite.

Under this arrangement, ISLA has adopted all GMSLA annexes that have been developed by PASLA and these will be made available to ISLA members via the ISLA website.

PASLA members will have access to the Legal Services section of the ISLA website.

In turn, members of both associations will have access to future annexes and associated documents that are developed jointly. This collaborative effort will also support development of annexes and addendums required to advance the growth of securities lending activity in the Asia-Pacific region.

In a joint statement, the two associations indicate this is an important move towards the digitisation of industry documentation, enabling member firms to access market-standard templates and to drive standardisation of market practice.

PASLA communication officer Paul Solway says: "This agreement is an important step forward in the harmonisation of documentation standards globally and delivers valuable new access market-standard templates, which promote the adoption of standard provisions across the securities lending market.

All the latest addendums and country annexes to the GMSLA are available to ISLA and PASLA members on the ISLA website.

resources to PASLA members.

"PASLA and ISLA are among the founder members of the Global Alliance of Securities Lending Associations (GASLA) and our collaboration on legal services reflects our broader commitment to working together for the benefit of all participants in the securities lending market."

ISLA CEO Andrew Dyson says: "The new legal services arrangement with ISLA [is] an important step for ISLA as it recognises that the GMSLA documentation suite is used globally by a myriad of market participants. It also supports ISLA's efforts to standardise documents in our market and will benefit members of our respective associations."

Malaysia's intraday short selling ban lifted on 1 Jan

Malaysia's temporary restrictions on intraday short selling were removed on 1 January.

The market's securities regulator, Securities Commission Malaysia, and stock exchange, Bursa Malaysia Berhad, say that this temporary suspension, which was due to expire on 31 December 2021, will not be extended.

This will lift current restrictions applied to intraday short selling (IDSS) and intraday short selling by proprietary day traders (PDT Short Sale).

Short selling activities will subsequently be permitted, but with enhanced control measures designed to promote market stability and orderly trading. This will include application of the "at-tick rule", which dictates that short selling orders must be executed at or above the best current asking price.

PDT Short Selling will only be allowed for securities listed as approved securities on the Bursa Malaysia Berhad Main Market (ie Day Trading Eligible Securities) and where the PDT already has an arrangement in place to borrow these securities. Naked short selling is not permitted.

The temporary ban on short sales was introduced on 24 March 2020 in the face of the COVID-19 pandemic. On 22 February 2021, the Securities Commission Malaysia and the stock exchange took a decision to extend this suspension until 29 August, and this was again subsequently extended until 31 December 2021.

FSB Asia group focuses on outsourcing risk

The Financial Stability Board (FSB) has conducted a virtual meeting to assess financial stability issues and potential vulnerabilities confronting the Asia-Pacific region.

The discussion focused on potential risks associated with service outsourcing and third-party relationships, including concentration of risk associated with dependence on a small number of outsourcing and third-party service firms.

The FSB launched a public consultation in November 2020 to gather industry feedback relating to risks associated with outsourcing and third-party relationships. This attracted responses from 39 organisations, including banks, insurers, financial market infrastructure companies, third-party service providers and industry associations.

The FSB released a summary of this industry feedback — responding to a FSB consultation paper entitled Regulatory and Supervisory Issues Relating to Outsourcing and Third-Party Relationships — on 14 June 2021.

In today's Regional Consultative Group meeting, FSB members also addressed financial stability implications presented by rapid innovation in financial services, linked to technology and other areas, and how financial supervisors can maximise opportunity generated by innovation and technology development while containing potential risks.

More broadly, the meeting reflected on macroeconomic risks at global and regional level, along with risks to financial stability presented by COVID-19 and policies designed to promote recovery from the pandemic.

The FSB has six regional consultative groups, each meeting twice per year, which bring together member and non-member countries to reflect on vulnerabilities affecting the financial system and steps to promote financial stability.

In line with this agenda, mapped out under the FSB Charter, today's meeting delivered an update on the FSB work programme and its expected output during the term of Indonesia's presidency during 2022.

The FSB Regional Consultative Group for Asia is chaired by Benjamin E Diokno, governor of Banko Sentral ng Pilipinas, and M Rajeshwar Rao, deputy governor of the Reserve Bank of India, respectively the central banks of the Philippines and India.

MarketAxess extends emerging and frontier markets liquidity to Egypt, Hong Kong and Serbia

MarketAxess, operator of an electronic trading platform for fixed-income securities, has announced that it has added Egypt (EGP), Hong Kong (HKD) and Serbia (RSD) to its Emerging Markets (EM) local markets offering.

Local currency trading, which now includes onshore Chinese debt (CNY), has grown to over US$147 billion year-to-date, up 20 per cent on the same period in the prior year. The number of active participants trading EM debt across the MarketAxess platform also reached a record of over 1,300 firms in the third quarter. Local markets across Latin America have been particularly active on the MarketAxess platform. With a record US$33.5 billion traded in the first three quarters of 2021, Mexico is the largest emerging market traded on MarketAxess.

Brazil is the second-largest emerging market with US$21.1 billion traded in the same period.

Kevin McPherson, global head of sales at MarketAxess, notes: "Investors are increasing their exposure to emerging markets, including frontier markets, in the face of increased demand for yield, broader index inclusion and easing of pandemic-linked monetary policy. Our volume growth through the first three quarters of this year is testament to that, and to the success of the unique all-to-all EM trading ecosystem that we have built to support them."

Maria Calderon, head of sales for Latin America, MarketAxess, adds: "MarketAxess has broadened the liquidity pool and helped to improve execution efficiency by delivering a range of protocols and tools designed specifically for how emerging markets debt is traded.

"Request-for-Market (RFM), Switch Trading and now EM Portfolio Trading have all seen rapid and significant adoption across both hard and local currency debt. These and other innovations have helped to deliver unique cost-saving and alpha-generation opportunities for our EM clients."

EquiLend, PASLA and RMA release 2021 Asia Pacific user guide

EquiLend has been working with the Pan Asia Securities Lending Association and the Risk Management Association to publish its 2021 Asia Pacific Securities Lending Market User guide.

Through this user guide and their other activities, the participating organisations indicate that they are committed to promoting open, transparent and efficient securities lending in the Asia Pacific region.

This promotes the harmonisation of regional market standards for securities lending, the integration of securities lending with ESG principles and the creation of a more open market for securities lending in China. It does so while recognising that different Asian securities lending markets are at varying stages in their development.

The user guide provides information and analysis on securities lending activities in 14 Asia Pacific markets. These are: Australia, China, China-Hong Kong Stock Connect, Hong Kong, India, Indonesia, Japan, Malaysia, New Zealand, the Philippines, Singapore, South Korea, Taiwan and Thailand.

The user guide is published on the EquiLend, PASLA and RMA websites.

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Navigating the twists and turns

Paul Solway, director and communications officer at PASLA, speaks to SFT about standout events during 2021, the focus of the Association's development activities and securities lending markets to watch during 2022

What were the standout events that most shaped the securities lending industry during 2021 from a PASLA perspective?

This has been a year in which bodies representing the global securities lending industry have become more coordinated and more focused on ESG.

As ESG continues to dominate the news and shape priorities for financial institutions, PASLA is proud to be at the forefront of the integration of securities lending with ESG principles. Alongside the Risk Management Association (RMA), we launched the Global Framework for ESG and Securities Lending (GFESL) in May this year. The aim of GFESL is to identify the touchpoints between ESG and securities lending and provide market participants with a framework for making decisions in those areas that align with their organisational ESG objectives.

On the back of GFESL, the five major securities lending associations globally came together to form the Global Alliance of Securities Lending Associations (GASLA). This Alliance aims to seek closer collaboration on global priorities for the industry — for example, to provide insight into

ESG integration and advocate for the benefits of transparent and regulated short-selling to liquid and sustainable capital markets.

Another initiative we have been focusing on heavily this year is the standardisation of documentation. This led to PASLA entering into a new legal services arrangement with ISLA in relation to the development of the Global Master Securities Lending Agreement (GMSLA) suite of documents, which becomes effective in January 2022.

The new arrangement has been agreed by the Boards of the two Associations and will facilitate the support and development of future annexes and addendums identified as requisites for securities lending activity in Asia Pacific markets, with input from specialists from the region.

PASLA's purpose remains unchanged — to promote open, transparent and efficient securities lending across the Asia Pacific and a key priority is supporting the continued liberalisation of financial markets in mainland China, especially as it relates to hedging tools and securities lending. As foreign investment in Chinese markets reaches record highs, in spite of this year's volatility, our members and prospective members are very focused on this market.

What were the primary risks and points of inefficiency confronting your members coming into 2022? How well has the industry managed these challenges?

Many PASLA members are global banks and financial institutions across Asia Pacific. They continue to manage a balancing act with limited resources and time as they navigate multiple markets in different time zones, higher revenue targets, funding and balance sheet constraints, cost pressures and heightened local and global competition.

We have seen some of our members remaining in product offerings that are more plain vanilla with an appeal to the mass market. In contrast, some participants have concentrated in niche markets that help generate higher returns — such as China, for example, where we expect the greatest expansion.

There is no right or wrong answer to this as long as sound risk management is applied in the decision-making process. As an industry, though, it is important not to set too many thin margin or loss-making precedents as it is hard to reverse decisions that may have wider market ramifications than anticipated.

What has been top of PASLA's priority list in terms of regulatory engagement during 2021? And work through your member workstreams and working groups?

Top of the priority list for PASLA would be the launch of the ESG framework and the formation [of GASLA] with our global peers as a unified voice that represents the securities lending industry. Our work with the International Securities Lending Association (ISLA) to bring conformity to the legal documentation repository is also high on our agenda to ensure there is a coordinated industry approach to meet market needs.

Despite the inability to travel and visit local regulators around the region, PASLA has continued to engage with regional exchanges. In Taiwan, we have seen the relaxation of some market rules to improve liquidity and activity. In Indonesia and the Philippines, PASLA has advocated and advised on local SBL exchange-driven platforms and short-selling regulations. In India, we have worked closely with market intermediaries to align with global standards by reducing previous tenure constraints for lending and borrowing contracts of 30 days to up to 12 months.

In China, PASLA has worked very closely with the Asia Securities Industry & Financial Markets Association (ASIFMA) to speak with Chinese regulators and exchanges on the utilisation of the recently available stock borrow facility via the Qualified Foreign Investor (QFI) channel. A number of initiatives are in the pipeline, including reporting of positions as well as creating a uniform interpretation of some rules that would disadvantage certain market participants. PASLA has also continued to work on the previous Connect reforms, but QFI reform outpaces that at this point.

A newly established PASLA Collateral Working Group has created a list of action points across each market to pursue advocacy and promote changes designed to encourage the use of local and global collateral in our region by interacting with exchanges and regulators. A good example of this is the gradual but important take up of Stock and Bond Connect listed securities as collateral, under a pledge structure. PASLA's other working groups have also delivered high quality webinars throughout the year on topics around ESG, collateral, China, technology and other market updates.

PASLA is committed to a more inclusive securities lending market and we were pleased to deliver a number of events on this topic during 2021. These included a virtual workshop on unconscious bias and an in-person get-together with PASLA members and market participants to officially kick off the PASLA Inclusion Network.

Which markets in the Asia-Pacific region offer strong opportunities as emerging and frontier securities lending markets? What steps are needed to develop these markets?

As mentioned previously, China has a number of initiatives in the pipeline and it will continue to generate strong opportunities in the years to come.

The Philippines working group at PASLA has continued to support the Philippines Stock Exchange (PSE) in addressing market concerns. One of the immediate priorities is the upcoming changes for short selling regulations to allow use of GMSLA and offshore collateral.

For Indonesia, the working group has assisted Bank Indonesia on its plans for introducing securities lending for Indonesian bonds.

PASLA is one of five regional trade associations to join GASLA in September. What are your objectives as a founder member?

GASLA provides a common voice for the global securities lending market, advocating for transparent and standardised practices that include the integration of ESG factors and the important digital evolution that supports efficient, liquid, and sustainable capital markets.

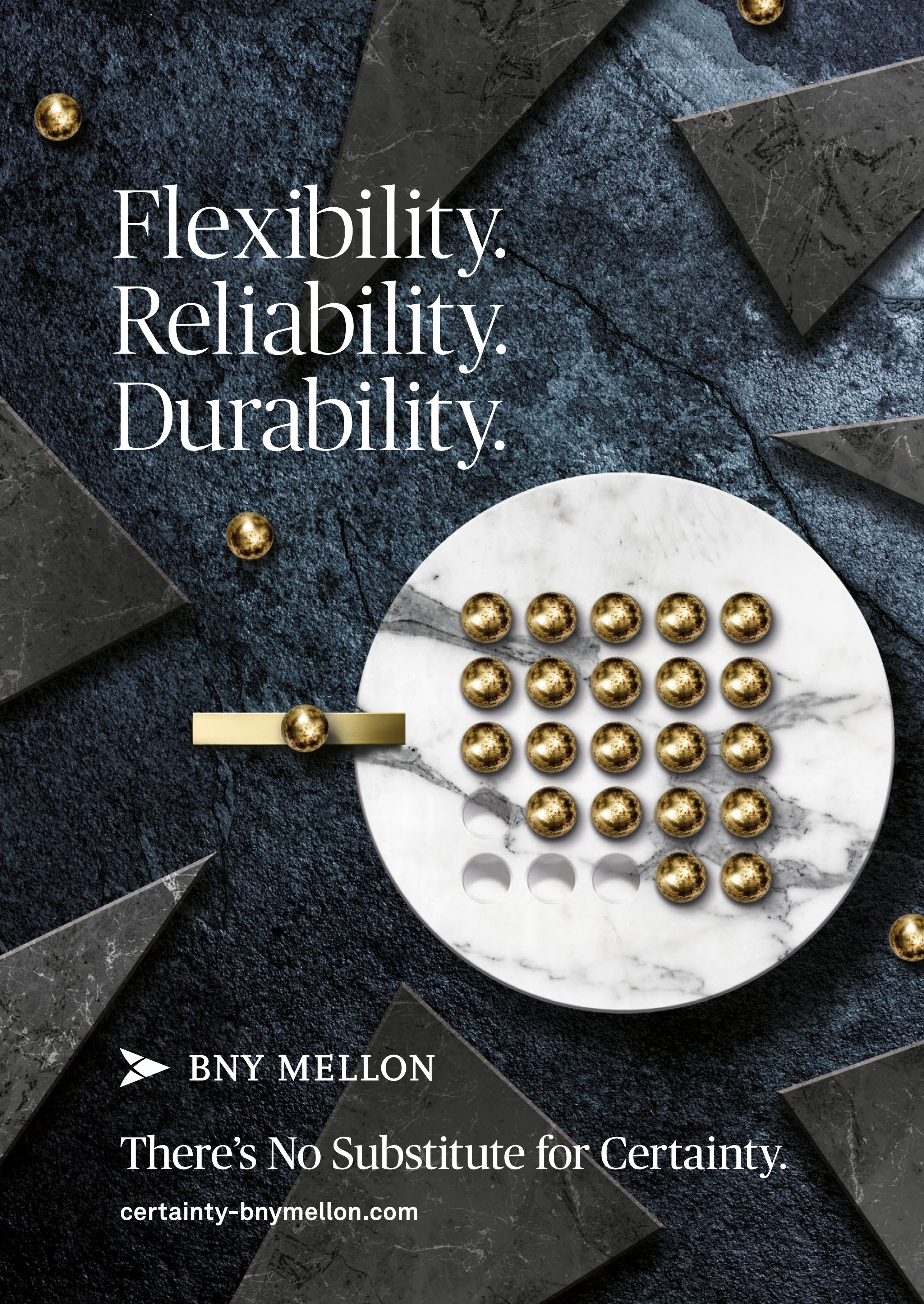
As a collective global voice for the securities lending industry, GASLA seeks to enable positive and impactful engagement with stakeholders, including regulators, policymakers, and standard-setting bodies in all regions. GASLA was formed with inclusivity as a core principle and welcomes securities lending and financial markets associations globally.

Many regional issues are morphing into global issues as regulators collaborate more closely across jurisdictions and regions while industry participants are thinking, acting and executing more globally. With the formation of GASLA, the aim is to avoid replication across different regions. This serves as a platform for knowledge sharing around the pertinent issues affecting us globally, such as ESG.

What is top of PASLA's working agenda moving into 2022?

China will be a top priority because of its size, progressive reforms and importance to our members. We will also be focusing on more emerging markets like the Philippines and Indonesia by engaging local regulators and exchanges as they develop their securities lending frameworks and regulations.

ESG will remain at the centre of what we do. Working alongside our GASLA partners will enable us to support the ESG agenda more effectively for our member firms as the road ahead twists and turns, but ultimately becomes clearer. ■



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Asia Pacific securities lending: Positioning for a strong 2022

Asia-based securities lending specialists reflect on the performance of APAC markets during 2021, the lifting of short-selling bans in Malaysia and South Korea, and prime opportunities for growth of lending activity in 2022 and beyond

Panellists

Jansen Chua
Senior managing director and head of securities finance APAC, **State Street Global Markets**

James Cooper
APAC trading head, agency securities lending, markets and securities services, **HSBC**

Sunil Daswani
Global head of securities lending, financing and securities services, **Standard Chartered**

Natalie Floate
Head of markets and financing services APAC, **BNP Paribas Securities Services**

Phil Garrett
Head of securities finance, Asia Pacific, **Northern Trust**

David Lai
Product manager, agency securities lending, Asia Pacific, **J.P. Morgan**

Paul Solway
Head of securities finance, Asia Pacific, **BNY Mellon Markets**

How do you assess the performance of APAC securities lending markets during 2021?

Jansen Chua: We saw a rebound in APAC market performance in 2021 versus 2020. This was driven primarily by strong short demand for Taiwanese (namely shipping and display panel issuers) and Hong Kong securities (HK-listed real estate issuers such as Evergrande Real Estate), capital restructuring (BHP in Australia) and a broad resumption of interest for South Korean securities where the short-sale ban, announced in 2020, was finally lifted.

Sunil Daswani: The Asian markets have been a real standout in 2021, with strong returns seen on both our discretionary and exclusive books. Borrower demand has grown over the period and continues to do so going into 2022, with most market participants bullish about prospects over the next 12 months. The big driver of much of this growth was the partial lifting of the short selling ban in South Korea, which not only drove activity in that market but also had the effect of buoying business across the region. We are optimistic that South Korea will continue its upward trajectory into 2022 and expect similar performance in Hong Kong, a market that very much returned to form in the latter part of 2021.

GC lending across many developed markets did soften through 2021, much of which was due to the meme-stock phenomenon that kicked off in the US in the early part of the year. Asia markets were not immune to this softening, which was particularly noticeable in Japan, although this was offset in part by increased lending volume over the record dates in that market throughout 2021.

Paul Solway: APAC securities lending for 2021 enjoyed stronger performance overall than 2020. Total securities lending revenue was up more than 30 per cent, with some markets in APAC clearly outperforming. Taiwan's securities lending revenue was up almost 200 per cent owing to the valuation of the panel makers and shippers, with the TAIEX ending the year as one of the best performing stock indices, up 23.66 per cent. Hong Kong and Malaysia were the other two markets that performed very well in 2021 in the securities lending space.

2021 was a thematic year, with lots of events driven by and related to COVID-19. Supply chain disruptions, energy shortages and chip shortages were some of the headwinds that impacted pricing and demand in securities lending. We have seen the high earners surrounding certain sectors like the shipping companies (Cosco, HMM, Wan Hai Line), the panel makers (AU Optronics, LG Display), rubber glove manufacturers (Top Glove, Sri Trang), and even the coal names (Banpu) — this was very consistent across all APAC markets. Corporate action and deal-driven names also played a role this year, with WH Group and BHP being two important earners in Hong Kong and Australia respectively.

In terms of weak earners, the only two markets in APAC where lending revenues have gone down were Japan and Singapore, which experienced a lack of specials this year. Singapore revenues were also impacted by the reduced dividend and scrip events for the major Singaporean banks in 2021.

David Lai: Taiwanese SBL growth was one of the key stories across the street in 2021. The industry has seen record trading balances as the market continues to grow in both onshore and offshore trading.

From an offshore perspective, I think it is fair to say that most supply has been centred around a select number of beneficial owner clients. So, it has been encouraging to witness the recent changes in our book composition and the increased dialogue that is taking place with our client base.

Korea lending activity has started to pick up traction following the last few KOSPI/KOSDAQ rebalances, which introduced some new IPO names into the short sell universe.

In Hong Kong, which is the most competitive market among lenders, global logistics, China technology, China property, and COVID/pharmaceuticals sectors continue to be the areas of focus. In 2021, we saw key specials in Hong Kong contributing significantly to our APAC revenue growth.

Phil Garrett: There were two key factors driving performance in APAC in 2021, namely China's regulatory clampdown on a number of domestic sectors and the eagerly anticipated return of short selling, albeit partially, in Korea.

At the start of the year, the focus was on US sanctions on investments in named Chinese companies deemed to have ties to the military. By mid-year, however, attention was turning towards the regulatory tightening across certain sectors in China, including technology, private education, gaming and most notably property. A potential liquidity issue emerged for China Evergrande Group and by year-end the credit situation was affecting most of the sector, causing fears of contagion and driving strong sector lending demand. China's clampdown created conditions which enabled market-wide short conviction not seen since before COVID. The Hang Seng Index finished down 15 per cent for the year, justifying the downside conviction.

Elsewhere Korea saw the re-introduction of short selling in May limited to constituents of the KOSPI 200 and KOPSI 150 indices, which saw strong demand driven by the likes of LG Display, HMM and Doosan Heavy Industries.

The sheer size of the Japanese market once again meant it was one of the region's top revenue generating markets despite being heavily GC with few notable specials through the year. Sector-wise, we saw strong demand in some e-commerce names while other demand came from convertible bonds and secondary offerings.

Taiwan and Australia also saw strong revenues, with both stock markets performing well through 2021. Taiwan was driven by technology, and primarily semiconductor names, as the PHLX Semiconductor Sector Index recorded an all-time high. Australia was a strong performer in the second half of the year as high vaccination rates saw lockdowns end and the economy start to improve. All eyes towards the end of the year were focused on the impending BHP unification event.

In summary, APAC lending performance was stronger year-on-year in terms of Return to Lendable for equity markets, outperforming other regions on that measure. The return to risk-on for short sellers, particularly in the second half of the year, was a major boost for revenue generation and a welcome trend going into 2022.

James Cooper: 2021 was both a challenging and exceptional year from an APAC perspective. The evolving COVID landscape globally impacted supply chains at all levels, with travel restrictions and the divergent global policies applied to tackle the virus creating a number of global, regional and country-specific opportunities. Structurally, short-sell bans were lifted in Malaysia and Korea, driving a resurgence in demand along with a number of broader market themes. Demand in both markets was strong, with Korea seeing balances rise to previous highs relatively quickly.

"The APAC markets continue to look very positive from a securities lending perspective. We continue to see inventory levels increasing, driven both by new investment mandates in the region and also new asset owners starting to enter securities lending."

James Cooper, APAC trading head, agency securities lending, markets and securities services, HSBC

The initial round of US sanctions in Chinese companies created some uncertainty in the market, but also opportunities for non-US asset owners and non-US entities. We noted that fees spiked on otherwise very liquid securities such as Xiaomi (1810 HK) as a result of the decrease in supply. In terms of China policy and the economy, we saw the regulatory tightening of technology companies, the restructuring of educational companies into non-profit organisations, and a liquidity crunch in the property sector — all of which drove security or industry-specific interest on the demand side.

Natalie Floate: Performance has been excellent in key revenue markets, particularly Hong Kong. This is a market that continues to impress us in terms of corporate activity and consistency of returns from special trading opportunities. In APAC, we are also constantly looking at South Korea, Taiwan and more recently at optimisation via the China Connect schemes.

Global financial markets have been subject to major fluctuations in liquidity and market pricing over the past two years, heavily linked to the impact of COVID-19 pandemic. What adaptations to working practices have you made to sustain and grow your APAC securities lending activity in this environment?

Solway: Our Trading Apps purchase in 2018 was key for our future-state resiliency, evolution and enhanced automation capabilities. The acquisition balanced low-touch automation with high-touch human influence, and this remains a fundamental focus for us in 2022. Working from home has also worked really well for us across the board; trading, relationship management and operations were all seamlessly moved from office to home working and they continue to work well for us.

Optionality continues for all our teams in both the front and back office, with staff able to choose which environment suits them in consideration of both their business-as-usual obligations and personal circumstances. Lack of travel has been a challenge for us but, again, technology has assisted in bridging any consequential gaps — although screen fatigue remains an issue for everyone.

Having a forward-looking location strategy to deliver local, on the ground solutions is another way we are making an impact in local Asian markets with our recent addition of a dedicated relationship manager in Seoul to serve our Korean clients. We also have further plans to expand product development and client service in 2022.

Chua: Flexible (or hybrid) work arrangements were definitely important adjustments that we implemented (and continue to invest in) to help provide support for our staff. Safety and well-being were clear priorities while balancing the need to minimise disruption to our programme, clients, and

“Specials will continue to be key to APAC revenues. Stress in the China property market will carry on, while the tech-heavy markets of Korea and Taiwan will continue to see volatility as both investor sentiment and macro influencers push and pull money in and out of this sector”

Paul Solway, head of securities finance, Asia Pacific, BNY Mellon Markets

counterparties. Virtual engagement with clients and prospects was a new activity that we had to adapt to, replacing the traditional travel-enabled face-to-face relationship meetings. This new mode of engagement required a shift in how we have traditionally managed relationships and was supported by instructor-led training classes for our teams and the use of external vendors to support client engagement events.

Maintaining engagement with our employees was also a key management consideration. Traditional methods of bringing people together (e.g. coffee meetings, 1x1 in-person meetings) had to be replaced with virtual engagements instead. This required more deliberate planning and coordination and a heightened focus on leveraging collaboration tools available across the enterprise.

Lai: First of all, the whole industry should be proud of how it has navigated through the last two years. When describing the industry to outsiders, the words ‘relationships’ and ‘communication’ have always been prominent and we have certainly seen these traits keep morale high and work processes efficient.

From a J.P. Morgan perspective, we were rather fortunate to have our Japan trading desk fully operational in January 2021. With three trading desks in the region, we were able to remain flexible as external factors constantly changed.

In Hong Kong, our Asia-Pacific headquarters, we brought all our staff together across two offices at the end of 2019. The cutting-edge technology of the new workplace allowed us to enhance our virtual connectivity and collaboration and it also enabled us to align our staffing parameters when this was deemed to be appropriate or necessary.

In which APAC markets do you identify new opportunities for growth of your lending business? What regulatory changes, and changes to market practice, are required to enable and sustain this market development?

Lai: At the start of a new year, we once again find ourselves excited about the prospects for the China market. The opportunities, challenges, and relevant developments have been discussed extensively in previous articles in this publication, so I will not repeat them here.

As mentioned earlier, the industry has demonstrated its resilience during the pandemic — working with each other, clients, counterparties, and authorities to address any requirements or concerns. As such, we are well-placed to participate in the China market under any framework that is agreed upon.

Daswani: There continues to be potential opportunities in APAC markets that will provide for growth in coming years. Timing is always a

“No conversation on opportunities in Asia would be complete without discussing China. There is some work to do here to open the market for foreign investor participation, but there may be an opportunity for an investor that is comfortable with the central counterparty risk”

Sunil Daswani, global head of securities lending, financing and securities services, Standard Chartered challenge, as generally the stakeholders in the local market will need to work with regulators to adjust or add regulatory language to allow foreign investors to participate. For example, in the Philippines there is a pending regulatory change to allow offshore collateral to be accepted and to recognise the industry standard Global Master Securities Lending Agreement (GMSLA). Whilst many hoped this would happen in 2021, it has yet to occur.

There has been increased dialogue with stakeholders in Indonesia in 2021. The focus has not just been on opening the equity market to foreign investors, but also potentially the fixed income market. The latter may initially focus on opportunities for domestic investors, but hopefully may extend to foreign investors over time.

No conversation on opportunities in Asia would be complete without discussing China. There is some work to do here to open the market for foreign investor participation, but there may be an opportunity for an investor that is comfortable with the central counterparty risk — which is the only option under current rules. This model, similar to what we see in Brazil, does restrict many lenders from participating owing to their own regulations on collateral, but this may present opportunities for some specific investor types, including onshore investors.

From a new investor perspective, we are already seeing interest from China insurance companies following the recent regulatory change which allows these investors to participate in securities lending. As always, the Pan Asian Securities Lending Association (PASLA) is leading the charge in advocating for change in Asia and both Standard Chartered and our JV partner eSecLending are supportive of these efforts.

Solway: We think both tactically and strategically in terms of counterparties, collateral markets and trade ideas or solutions. The art is to nimbly navigate the different permutations that exist between these evolving parameters. The region remains diverse, fluid, and opportunistic, so having tactical options within existing open markets is key. Collateral is also a significant factor, with major considerations being cash versus non-cash, pledge versus title transfer, and RWA-friendly assets versus less capital-efficient securities.

Last year we spoke about new market aspirations such as China, Philippines and Indonesia. Not much has changed for these markets in the past 12 months, but we continue to work with PASLA and others to advocate and influence moves for regulatory change, market openness and harmonisation across Asia. With our successful delivery of China Stock Connect as collateral within agency lending, our sights now turn to China Bond Connect in 2022 in the expectation that this additional collateral flexibility will provide further financing solutions to the street and will underpin spreads and grow utilisation rates.

“There were two key factors driving performance in APAC in 2021, namely China’s regulatory clampdown on a number of domestic sectors and the eagerly anticipated return of short selling, albeit partially, in Korea.”

Phil Garrett, head of securities finance, Asia Pacific, Northern Trust

In the meantime, we remain strategically focused on adapting our models, where necessary, to make it easier for counterparties to trade through and with us. Linking products and services will allow us to leverage our franchise, which will not only add real value for our clients but also foster market efficiencies and drive meaningful price discovery in local markets.

Garrett: The securities finance industry has had China in its sights for over a decade. Promising developments in the China Qualified Foreign Institutional Investor (QFII) scheme to allow securities lending led to much optimism in 2020. However, idiosyncrasies around the operating model have meant that any meaningful participation for offshore lenders is extremely limited. Ongoing regulatory engagement through industry bodies such as PASLA and Asia Securities Industry & Financial Markets Association (ASIFMA) will hopefully enable modifications that will allow for full access to China through a more compatible model in the future. Whether this will happen in 2022 is, admittedly, doubtful.

Other markets to watch out for are Indonesia and the Philippines. Both markets have been stop-start on progress towards a viable SBL model for offshore lenders. For Indonesia, there were signs of regulatory re-engagement towards the end of the year, while in Q1 the Philippines announced the intended launch of rules and regulations for short selling. However we are still waiting for this to happen and both markets remain on hold at the time of writing.

The potential lifting of the remaining short-sell ban in Korea will also provide additional opportunity and we await further news from the regulators on this.

Cooper: Collateral mobility and optimisation remains a key focus in APAC. We continue to see demand for a widening of acceptable title transfer assets such as corporate bonds and ETFs, along with the acceptance of non-standard or ID market [where foreign investors are required to have an investor ID registration to trade and invest] securities such as Korea, Taiwan and Stock Connect — and then, more generally, the pledge structure is generating strong interest. As spreads narrow on historically higher fee lending markets, collateral costs are becoming increasingly important.

Local regulations for some of the ID markets present very specific regional opportunities, along with wider use of non-cash collateral globally and particularly in APAC. We have noted collateral convergence on the borrower side, with optimisation viewed more holistically across the whole business, and this has created new opportunities across business lines and also across regions. As an agent lender, we need to work closely with our clients to maximise these opportunities within their accepted mandates and risk profiles.

What impact is technology development, and parallel standardisation and digitisation of securities lending practices, having in the APAC region?

"The whole industry should be proud of how it has navigated through the last two years. When describing the industry to outsiders, the words 'relationships' and 'communication' have always been prominent and we have certainly seen these traits keep morale high and work processes efficient."

David Lai, product manager, agency securities lending, Asia Pacific, J.P. Morgan

Solway: The region remains a collection of unique markets that have their own rhyme and reasons for rules, regulations, and activity. However, systematic solutions and controls are now in place for all nine active markets across APAC. Trading Apps remains our differentiator, enabling our traders to focus on the high-value and high-touch trades across both equities and fixed income. Despite spreads remaining under pressure, our balances at BNY Mellon grew in 2021, with records being broken in Japan during seasonal periods in the past year and technology being an enabler of this activity. Using technology in operations is also very much our priority, not only lowering the potential for human error but providing volume and scale that matches off against quant-driven, high-volume trading strategies that are now the new norm.

Lai: J.P. Morgan continues to focus on innovation and meeting the future demands of our clients. Our effort in digital evolution combines artificial intelligence, blockchain technology, and thought leadership to deliver innovative solutions for our clients across our securities financing products. The real-world application of blockchain technology has begun to pick up the pace. It is incumbent for J.P. Morgan to remain integral to this ecosystem and provide liquidity to the market. From a practical perspective, the APAC region still has an overseas nexus, whether from a high-quality liquid asset (HQLA) or a USD cash aspect or a support framework owing to the necessary 'round trip' or 'follow the sun' processes inherent in our business.

As such, any standardisation or technology development that reduces (or in some cases completely removes) the need for tracked and confirmed movements and post-trade reconciliations will be welcome.

What are the key issues for the APAC securities lending community in promoting high ESG standards across the SBL transaction value chain?

Daswani: More words were written in 2021 on securities lending and ESG than ever before and it continues to be a hot topic in 2022. We continue to believe that ESG and securities lending can be appropriate companions and the industry associations are working hard to give investors the knowledge and information to ensure comfort in managing these two activities in tandem. In fact, the Global Framework for ESG and Securities Lending (GFESL), published by PASLA in May 2021, led the charge in providing a structure for investors to follow. More recently, a number of industry associations have formed the Global Alliance of Securities Lending Associations (GASLA) to continue the work and focus on ESG solutions for the industry, among other important themes.

At Standard Chartered, we have been part of a regular

"We are expecting more corporate activity in the region as long as conditions remain accommodating. For example, Hong Kong should continue to benefit from new equity listings and IPO demand."

Jansen Chua, senior managing director and head of securities finance APAC
State Street Global Markets

dialogue with clients and prospects about ESG and securities lending. We believe that securities lending should not be an impact to success in meeting an investor's ESG requirements. Many years ago, our partner eSecLending introduced Proxy Value that provided clients with data on voting materiality and securities lending revenue to better inform the decision about whether to recall a security from loan to vote. As you would expect, this has now evolved to include other elements of the environmental and sustainability agenda to add important additional colour to the information available to clients and fully support the ESG agenda.

Collateral screening has always been something that we have been able to do, primarily due to the segregated nature of our collateral accounts – the client is truly in control of what is taken as collateral and we can support changes as necessary. The main focus of client discussions here has been around managing this element of the programme in a way that is scalable. Thus, the introduction of ESG indices that can be supported by triparty collateral agents has been a particularly strong step to demonstrating adherence to ESG principles in collateral management.

Lai: ESG remains a focus topic for the global industry so, being mindful of the material in the public domain, I reiterate that our approach with all our clients is to understand any specific requirements they may have regarding their lending programme.

This might seem rather a basic statement, but it is the first step in initiating the multitude of programme parameters within the J.P. Morgan Agency Securities Finance platform that allow our clients to customise their agency lending programme. This will impact the range of assets and possibly the rate of return of a lending programme — which our analytical tools will help to highlight. Understanding a client's requirements and discussing the potential impact is the basic fundamental backbone of our business.

If there are client requirements related to the associated collateral, this will also impact the lending programme and processes involved. But, similar to above, these challenges can be worked through with active and clear communication from all parties.

Chua: We continue to see increasing interest in the application of ESG principles to securities lending activity. However, there are still a number of challenges that currently inhibit faster adoption into lending programmes, chief of which is the lack of a clearly defined and widely agreed set of standards among investors. For example, what is considered 'eligible' collateral for one investor may be considered 'ineligible' for another. This results in the need for customisation, which in turn prohibits the application of scalability to the processes of lending agents, borrowers and triparty collateral providers.

"Our role as agent is critical to highlight that a fund's core ESG objectives can be stretched into their securities lending mandates in a complementary way."

Natalie Floate, head of markets and financing services APAC
BNP Paribas Securities Services

We also see growing interest in steps to promote transparency into lending activities. Investors are asking questions about their lending activity. For example, who are the ultimate borrowers of the securities? For what purpose are the securities being borrowed? And are these purposes (e.g. short selling) aligned with their own ESG principles? We view peer-to-peer models as potentially a means to achieving this transparency objective between the principal lender and principal borrower. Traditionally, intermediaries such as the prime brokers and broker-dealers have stood between these principal parties. To address client demand, State Street introduced Direct Access, our managed peer-to-peer programme, in late 2019, enabling direct transactions between our lending and borrowing clients.

Investors have also expressed growing interest in exercising their voting rights for their securities lending portfolios. The desire to maximise lending returns can, at times, appear to be at odds with the need to exercise oversight and governance obligations over issuer companies. There are a range of tools available – such as recalling securities, restricting specific securities, setting limits on lendable amounts – whereby agent lenders can help beneficial owners bridge these two requirements.

Solway: As articulated in many webinars, the focus is currently on proxy voting, collateral and, as always, transparency. I have argued that most, if not all, current ESG concerns have been considered and adapted for in most modern agency lending programmes. At BNY Mellon, we have frameworks in place that give optionality across proxy recalls, collateral/lending restrictions, big data reporting, real-time benchmarking and active parameter screenings. The key challenge is finding sweet spot ESG requirements and standards across a multitude of clients who are all still navigating through their own corporate ESG mandates —and that may not have yet considered the niche impacts to securities lending programmes.

If all clients suddenly restricted lending for proxy votes, there would be a serious impact on supply in certain names and markets — that is obvious, especially in markets like Japan where proxy/AGM events are very prevalent. It is important to advocate for pragmatic approaches. Not all electable events are significant enough for all shareholders and so stewardship obligations may differ. At BNY Mellon, we are currently working to standardise some ESG collateral profiles for clients to leverage. As a leader in the triparty space, we have an obligation to be a first mover in providing our clients with pragmatic screening options for both lending and collateral.

Floate: ESG is not a new topic in APAC. It has been a key focus for beneficial owners that are long-standing participants of the securities lending market. This has positioned us well, enabling us to adapt, adopt and implement our lending clients' ESG objectives, which are already mature and well established in their core portfolios, before being stretched into ancillary activities such as securities lending.

In this regard, we see the role of the agent as critical. Speaking for BNP Paribas Securities Services, our clients look to us as their agent to see what it is possible to implement and to guide them on the implications — particularly in working through the value chain with borrowers and collateral managers. Proxy voting was the first element discussed from Australia and now we are seeing collateral screening as the next natural phase for ESG across APAC. Securities lending is not always considered by beneficial owners when they think of ESG. As such, our role as agent is critical to highlight that a fund's core ESG objectives can be stretched into their securities lending mandates in a complementary way.

How do you assess the outlook for APAC securities lending markets for 2022?

Garrett: The macroeconomic themes that have played out in 2021 will continue to have a heavy impact on borrower demand in APAC for the coming year. China's common prosperity goal will heavily influence stock market conditions not just in China and Hong Kong, but also in regional markets tied to the fortunes of the world's number two economy.

Therefore, we expect volatility and strong short-side interest to continue for the foreseeable future across the region. That said, we may see some easing in policy to avoid any systemically-impactful defaults. More recently, there has been much talk about an easing of the three red lines policy in the property sector as the government seeks to avoid a wider shock to the Chinese economy.

The reality of rising interest rates will undoubtedly increase volatility across global equity markets and we have already started to see this play out. Even those stock markets which fared well through 2021 are likely to see upward momentum checked in the face of this new environment. This will provide additional motive for more short-side positioning.

There is hope that at some point in 2022, Korea will lift the remaining short-selling ban to allow inclusion of all indices. As we saw with last year's actions, this should provide an opportunity for lenders and borrowers to increase returns from this market.

Solway: Against the backdrop of ongoing and remaining risks from COVID-19, there will be big challenges alongside some surprising and significant opportunities. I fear for some conservative approaches in terms of regulatory or exchange actions against any extreme market movements that may play out. At the very least, certain hopes for market infrastructure progress in emerging markets may see continued procrastination, delays and postponement. The deep, liquid markets will continue to see the best activity; Hong Kong and Japan will continue to dominate. The question will be whether Korea and Taiwan will continue their positive trajectories without impediments or restrictions that cause a drag on revenue opportunities.

Specials will continue to be key to APAC revenues. Stress in the China property market will carry on, while the tech-heavy markets of Korea and Taiwan will continue to see volatility as both investor sentiment and macro influencers push and pull money in and out of this sector. Cash reinvestment is going to be one of the larger focus areas in 2022 for clients. Despite APAC naturally having a lighter cash collateral usage, yield curves are heading north and so nimbler clients will see opportunities and benefits from surprise changes to US and European monetary policy that may play out this year.

Questions remain over whether it will be a global soft or hard landing. Will the US economy be able to handle 1 per cent interest rates? These, and other factors, will decide how 2022 goes for most of our financing community.

Lai: As we begin 2022, we see challenges and opportunities in the securities lending market. In Hong Kong, we expect to see more Chinese companies listing on the Hong Kong exchange. It remains to be seen if SBL activity on these names will remain a key revenue driver.

Korea continues to work its way back to pre-short sell ban levels. While short selling is constrained to a universe of eligible names, Korea represents one of the higher fee-generating markets in APAC, so we are optimistic that this will be a key market for us going forward.

As outlined in our response to an earlier question, the securities lending market will continue to evolve with a focus on automation and product diversification.

Cooper: The APAC markets continue to look very positive from a securities lending perspective. We continue to see inventory levels increasing, driven both by new investment mandates in the region and also new asset owners starting to enter securities lending.

We are also seeing a number of local Asian markets continuing to develop their infrastructure to introduce securities lending. Following the rule change in late 2020 which allows qualified foreign investors (QFIs) to transact in onshore SBL, China continues to be a key focus, especially for agent lenders, in terms of providing solutions for both onshore and Stock Connect securities. The increased investment in APAC has also created a need to finance new assets, which might be harder to mobilise than those in some other developed markets. The growth in both the pledge structure and tokenisation offers potential solutions for those historically locked in assets.

Chua: We believe APAC markets are generally positioned well for another good year in 2022. We are expecting more corporate activity in the region as long as conditions remain accommodating. For example, Hong Kong should continue to benefit from new equity listings and IPO demand. There are some uncertainties that may create disruptions, namely the Federal Reserve Board's (as well as several regional central banks') stated intention to raise interest rates as well as broader implications of geopolitical events.

Daswani: We are optimistic about the region in 2022, evidenced by the strong bidding we have already for exclusive supply for the coming 12 months, seen by auctions eSecLending ran themselves, and on our behalf, in late in 2021. Returns in South Korea and Hong Kong should continue to strengthen and, similar to what was witnessed last year when the South Korean short selling ban was lifted, we expect that trend to spill over into the other key markets in the region. We remain hopeful that progress will be made in opening up both Indonesia and the Philippines for offshore lending later in the year.

What is top of your development priorities as an APAC securities lending division for the 12 months ahead?

Lai: Last year's Securities Finance Times Asia Handbook announced that J.P. Morgan was the first agent lender to accept China A-shares as collateral for a securities finance transaction conducted through the Hong Kong and China Stock Connect. The logical expansion is to include Bond Connect securities in our acceptable universe of collateral. Not only would this expand to seven the number of APAC domiciles in our acceptable fixed income collateral universe, it naturally builds on the official 2017 launch of Bond Connect.

Over the next 12 months, our team will focus on the further build out of the J.P. Morgan Agency Financing product set, giving APAC clients the ability to solve for all liquidity objectives across a single platform. The platform already offers significant efficiencies in terms of the legal framework, liquidity access, and operational support model, but the development of order management and optimisation functionality will serve to strengthen the economic proposition for outsourcing financing activity.

As a direct result of the next phase of the uncleared margin regulations due in September 2022, the scope of the J.P. Morgan collateral mobilisation and management tool, Collateral Transport, introduced in last year's Securities Finance Times Asia Handbook, will be widened further to be fully custodian agnostic. This will enable the client to consolidate its view on inventory across multiple custodian venues and optimise collateral flows as necessary.

Cooper: As an agent lender, optionality is key to monetise opportunities as and when they exist. This includes having the infrastructure in place to lend in new markets and the ability to accept wider collateral types. This also involves maintaining close and constructive relationships with beneficial owners to discuss time-sensitive trade opportunities. In a market of uncertainty, it is important to focus on those elements that are controllable and product enhancements that enable us to optimise performance for our clients' portfolios that we are entrusted with.

Solway: People, systems, products and clients remain our focus in 2022. Without talented people, smart systems and evolving products, we cannot solve for the needs of our regional and global clients. We will continue to invest in and care about our people to execute a strategy that ensures resiliency both locally and regionally.

Targeting and optimising high-impact securities remains at the forefront of our strategy, from institutional high net-worth or retail clients. Additionally, untapped and new sources of supply are the jewels in the crown these days. Scalable same-day trading is also an area where we want to invest and provide solutions in 2022 as regulations and settlement cycles tighten, with associated penalties only going one way — up.

Developments in collateral mobilisation continue to deliver opportunities in the Asia Pacific

J.P. Morgan's Bhavna Haswani, product manager, collateral services, and Will Jeffries, platform sales, triparty collateral services, examine how clients are looking to reduce friction in core collateral markets and increase mobility of trapped assets in new locations

Despite another year marked by COVID-19 pandemic challenges, 2021 continued to provide meaningful developments within securities lending and collateral management. Ongoing regulatory developments mean that clients are continuously looking for opportunities to reduce friction in core collateral markets and increase the mobility of trapped assets in new markets. Trends in creating an integrated collateral ecosystem remain critical for the future development of collateral management services during 2022 and beyond. We will examine some of the developments in how we support our clients.

Australia

Australian participants have long had the benefits of financing securities through the global triparty platform. However, more recently, the growth has been derived through the utilisation of the J.P. Morgan local programme, where clients can leverage global technology and infrastructure, blended with local laws and regulatory oversight to create a targeted Australian triparty ecosystem.

We saw a 100 per cent year-on-year collateral balance growth in 2021 as a result of partnerships with the local Australian-based banks, broker-dealers, agent lenders and buy-side firms to optimise collateral portfolios and reduce operational risk within the local time zone. The benefits of triparty are most evident through the network effect of many users interfacing within the same platform and J.P. Morgan has continued to invest in the local Australian platform to ensure we can achieve a higher level of efficiency for both borrowers and lenders.

With J.P. Morgan Direct Custody and Clearing acting as our local settlement agent, this further enhances our operational and settlement efficiencies in managing local securities. To add to this, we continue to support record date allocations for Australian securities and provide franking credit notifications for onshore entities on fully franked dividend events, adding significant value to local borrowers.

Regarding the impending implementation of Phase 6 of the Uncleared Margin Rules, J.P. Morgan is leading the way for local Australian newly in-scope firms with respect to the Segregated Initial Margin operations. Our newly released Collateral Transport system has assisted buy-side clients in selecting and mobilising securities for initial margin and variation margin obligations, as well as identifying securities that may be better utilised through securities lending transactions.

As we continue to enhance our local offering, we are looking at new and better ways to leverage our global platform and connect Australia with the rest of the world. For example, we are currently working on an initiative to reduce settlement friction between local Australian entities and their global affiliates. Additionally, as we continue to see pledge adopted in the global securities finance space, we have adapted pledge documentation under New South Wales law specifically for the Australian market.

Japan

The size and importance of Japan to the global securities financing markets can never be underestimated. In 2021 we increased our commitment to the local market. We now have an unrivalled full-service triparty team onshore supporting our Japanese clients across sales, client service, product and onboarding.

In addition to our ability to support record date allocations for Japanese Government Bonds (JGBs) and Japanese equities, recent operational enhancements have simplified our income payment process directly to the borrower from our local agent, providing streamlined reconciliations and automation for collateral providers.

We have seen domestic clients looking to trade under local pledge structures, an area that has become increasingly important as global pledge structures start to increase in prevalence. Using experience developed from our local Japanese financing platform, we recently adapted our global pledge documentation and internal operational processes so that we can now support the perfection of pledge over Japanese securities for cross-border transactions. This recent development ensures global lenders receiving Japanese securities under pledge structures have a valid and perfected security interest compliant with local laws and operating guidelines.

Connecting Japanese lenders with offshore borrowers as they continue to search for new opportunities in the global marketplace continues to be our focus and an important growth driver. Similarly, we continue to support global lenders looking to access new areas of demand by accessing Japanese borrowers.

Hong Kong China Stock Connect

The most significant development over the past 12 months has been the increasing lender participation. Many lenders have been able to complete their enhanced due diligence and take advantage of the unique opportunities available to finance this new market. One of the key drivers of increasing lender participation has been the development of an end-to-end collateral liquidation solution that J.P. Morgan can offer to clients through our internal affiliates and external execution brokers, should clients wish to have an independent third-party liquidate collateral.

China remains the market to watch as access routes develop and Chinese securities enter the mainstream, driven by continued market development and index inclusions. We are staying engaged with our clients on the best way to support their collateral mobilisation requirements as the market evolves.

Today J.P. Morgan supports clients looking to utilise China A-shares acquired through the Stock Connect programme. We can do so through a standard triparty pledge structure where J.P. Morgan acts as the custodian. However, due to certain market requirements specific to China Stock Connect, a more practical solution was to develop a custody-agnostic solution.

This has allowed collateral providers to increase the range of securities they are able to mobilise and significantly reduce the friction and settlement risks in moving securities into a triparty structure. Over the past 12 months, we have successfully integrated with several third-party custodians and allowed clients to optimise Stock Connect securities in the most efficient way possible.

While we have an unwavering commitment to developing the A-share market, it's extremely hard to ignore the size and breadth of the Chinese Government Bond (CGB) space. We are currently conducting analysis and reviewing the optimal way to support this market for clients. We would welcome any engagement from clients looking to mobilise CGBs as initial margin or through securities finance transactions.

The Road Ahead

Collateral mobilisation will remain a core part of our ongoing dialogue with clients as we progress through 2022. J.P. Morgan will stay focused on developing and enhancing existing structures, allowing clients to extract further efficiencies and capitalise on new opportunities. The value of reducing friction in the movement and processing of securities means that even small efficiency gains can be significantly impactful and immediate. All the while, larger industry initiatives continue to evolve. We are excited not only by what the future holds for new and existing markets in Asia Pacific, but also how technology will evolve and shape the future of collateral management in the region. ■

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Product Manager, Collateral Services
J.P. Morgan

Will Jeffries
Platform Sales, Tri-party Collateral Services
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ESG expands into collateral management

With new regulations and changing attitudes, ESG continues to accelerate from concept to implementation for securities lending and collateral management. State Street's Sam Edwards and Roy Zimmerhansl of Pierpoint Financial Consulting, examine the industry's roadmap

Since environmental, social and governance (ESG) was coined in the study "Who Cares Wins" in 2005, it has grown from a niche consideration to a mainstream trend. It is now a norm for institutional investors to integrate ESG considerations into their investment decision making, seeking positive returns while keeping in mind the potential long-term risks to the performance of their assets.

However, the application of ESG to securities lending has been slow. There is no standardised framework which creates challenges and makes it difficult for industry participants to navigate the 'different shades of green'. Regulation is set to help overcome these challenges and make green labels meaningful for investors.

For example, the European Union's Sustainable Finance Disclosure Regulation (SFDR), which went live in March 2021, aims to establish transparency requirements for financial market participants on the integration of sustainability risks. It also helps participants focus their efforts on the consideration of adverse sustainability impacts in their processes and the disclosure of the sustainability features of financial products.

With new regulations and changing attitudes, ESG's momentum continues to accelerate. State Street sees this as an opportunity to differentiate ourselves and provide value to our clients. We are moving forward to enable ESG ratings in our Collateral+ triparty service and we are excited to see progress across financial services.

Industry dialogue

In the following discussion, Sam Edwards, head of APAC Collateral, State Street, and Roy Zimmerhansl, practice lead, Pierpoint Financial Consulting, discuss the industry roadmap for accelerating ESG from concept to implementation with a focus on the collateral side of the trade.

Sam Edwards: At State Street, we have been developing our new Collateral+ platform, with ESG at the heart of the design process. Why has ESG implementation in securities lending and collateral been so slow within the financial services space?

Roy Zimmerhansl: There are three key aspects that have influenced the initially slow, but now rapidly accelerating, emergence of ESG. First, as with many new concepts, it took some time for investors to acknowledge, accept and then integrate ESG factors into portfolio construction. Second, critical to all new initiatives, the necessary data and tools have taken a while to become widely available. Finally, in the absence of regulation, there is no standard definition of ESG, which is leading to different interpretations and measurements with multiple indices. This makes comparisons difficult.

Nevertheless, the baseline of ESG in securities finance is gaining clarity. This reflects both the wider investment community ecosystem and specific initiatives within this sector.

Sam Edwards: While regulatory changes have kept financial services firms busy over the last decade, there are clear benefits to be derived from industry collaboration to enact change. The approach to managing collateral schedules is usually based on a legacy approach that enables limited changes based on security-level exclusions.

The Collateral+ platform is developing digital schedules that will be easier to update and manage. As part of this, we are advocating the introduction of ESG ratings. To be eligible, a collateral receiver sets a minimum rating level the collateral must meet. We can envisage a dynamic approach, whereby changes to ratings immediately update the collateral eligibility set.

When advising your clients, what are the key points Pierpoint looks to for the implementation of their approach?

Roy Zimmerhansl: Most observers acknowledge that sustainable investing is more than a passing trend. Vendors are rising to the challenge by either enhancing existing products or introducing new ones. Inevitably, this means there will be an array of service providers feeding institutional investors with

ESG-focused ratings for portfolio oversight. In our experience, lending investors are at various stages of their journey in applying guidelines to their collateral. This will be particularly acute for retail-oriented ESG funds such as exchange traded funds (ETFs) or mutual funds.

Imagine two ESG-labelled funds that lend securities. The first one markets an end-to-end ESG solution including securities lending collateral and the second one ignores collateral. The latter scenario is ripe to be challenged for greenwashing.

Meanwhile, consider pension funds for government employees such as the Local Government Pension Schemes in the United Kingdom. Many trustees feel an additional obligation, beyond service to their members and their stewardship requirements, and so are more likely to push the ESG agenda and support global initiatives. This will challenge collateral platform operators – they must be willing to connect with multiple client-selected ratings providers, which is likely to offer a range of acceptable connected ratings vendors.

This flips the traditional method used for pricing where collateral platforms determine the best data providers, add them in efficiently and use those prices to inform the collateral valuation process. Here, there are a few sources feeding many users. In the case of ESG ratings, lenders will demand conformity with the ratings provider used to filter their portfolio investments.

Sam Edwards: At State Street, we will provide access to multiple sources of ESG ratings via established market utilities to enable clients to customise their approach and evaluate any differences. This will allow us to enable change while working on the second step, the addition of new providers of ESG ratings.

Providing access to ESG ratings sources will provide asset owners and collateral receivers with the tools they need to address the wishes of their stakeholders. This will enable our clients to enable customisation of each of E, S and G to match investor preferences, through creating their own bespoke ratings scales.

How do you see this playing out in the next few years?

Roy Zimmerhansl: Investors are continuously refining their approach to the wider sustainable finance initiative. This fluid effort demands a multi-step approach to collateral. Inevitably, this will need to deliver direct control for end-users to reflect their specific E, S and G preferences, or combined ESG criteria.

However, service providers will need to take an agile approach to collateral management. The end objective should be high automation facilitating mass customisation by users.

Sam Edwards: With the ever-increasing need to focus on the environmental aspect, we can see the E playing a significant role over the next decade. But there are also other factors that need to be addressed across the spectrum from asset owners, lenders, borrowers, triparty agents, regulators, rating providers and industry forums.

Where do you see the driver for implementation coming from, and why?

Roy Zimmerhansl: The pervasive nature of ESG is what makes it different. For example, although changes resulting from the Securities Financing Transactions Regulation (SFTR) were driven by regulators and approved by politicians, the reality is that the impact was largely felt by financial intermediaries.

We see many stakeholders wanting to influence the development of ESG. But when you consider local and regional differences and priorities, skewed by political agendas, it’s easy to see why there is no straight line to a unified global vision.

Securities finance leaders and influencers must create conditions where participation and inclusion are encouraged and even demanded. We need to listen before deciding and our actions should be incremental and continuous. Meanwhile, technology must be leveraged to deliver the needs of both ends of the user chain, via the intermediaries that are fundamental to daily financial market infrastructure operations.

Hong Kong leads growth in Asia revenues

In reviewing recent developments in APAC securities finance, Jeff Coyle, head of Hong Kong agency trading, securities finance, Northern Trust, notes that Hong Kong continually catches the headlines and drives revenues

2021 was an impressive year for securities finance markets in Asia Pacific (APAC). The partial return of short selling in Korea, a stellar performance from Taiwan driven by soaring valuations, the BHP unification event unfolding in Australia, and the usual reliable stream of income from the regional behemoth Japan, all contributed to the best regional performance as measured by revenue generated per lendable assets.

However, it was Hong Kong that continually caught the headlines and produced the most revenue in APAC. This market contributed more than 30 per cent, or US$264 million, of the total regional earnings for the year, according to IHS Markit data. So what are the key dynamics propelling this market?

Hong Kong's global connectivity, open capital markets and its position as the international investment gateway to China — notwithstanding the growing importance of Qualified Foreign Institutional Investor (QFII) and Stock Connect access — means that it is affected both by global financial events and economic developments on the mainland. Hong Kong deserves a special focus from any lender that has aspirations to lend in China and may be viewed as a proxy for how securities lending could eventually play out on the mainland, if and when material offshore investor participation becomes viable.

There are a number of elements that have shaped borrower demand in the Hong Kong market over the past few years — and these will continue to do so over the immediate horizon. The longest enduring factor is the US-China trade war, which began in mid-2018. The imposition of import tariffs has impacted many Chinese companies, including those that list on the Hong Kong exchange. As the US expanded its actions, some sanction measures were introduced. 2021 began with the eyes of the securities finance market focused on the US Executive Order (EO) 13959, which prohibits US investors from holding shares in named Chinese companies deemed to have ties to the Chinese military. For Hong Kong listed companies captured by the EO, this created navigational challenges and resulted in elevated lending fees in some securities for those lenders still able to capture demand.

Another impending outcome from the trade war will be the potential delisting from US exchanges of a large number of Chinese companies. Over 200 Chinese companies could delist from the New York Stock exchange and NASDAQ over the next three years. Hong Kong is a likely beneficiary of this action and could well see a fair share of the roughly US$2 trillion coming to list on its shores.

Although the move will deny companies access to the vast US capital market, much cross-border investor money will surely follow the migrated listings, particularly as many of these companies have significant growth prospects. IPO listings, IPO lock-up expiry events, as well as MSCI and FTSE index rebalances resulting from the new listings, will all be favourable to increased securities finance activity. In 2021, Hong Kong was responsible for approximately 20 per cent of the US$550 billion of capital raising activity in APAC, generating revenue for lenders of those securities through these events. The additional listings could elevate this activity to another level.

Regulation, as always, plays an important role, with securities finance markets continually needing to adapt. Among other developments, investors have been required to adjust to updated industrial policies from China by mid-2021. The second half of the year brought a marked rise in short interest and a clear change in short-side conviction in Hong Kong. This resulted not only in increased borrowing demand, but also drove a specials environment to a level not seen since before COVID — with technology, private education, gaming, finance and property among the factors that attracted most interest. Additionally, we saw high borrow interest leading into IPO lock-up expiry in certain names as some investors sought to sell their holdings at the first available opportunity. By year-end, Hong Kong's Hang Seng index (HSI) was down 15 per cent and was one of the poorer performing indices in APAC — which vindicated the downside conviction.

At the turn of the year, there was growing optimism that some policy measures may be revised, therefore, calming the market and allaying investor fears about systemically impactful defaults, particularly in the property sector. The change in outlook, coupled with low valuations, gave investors renewed confidence and allowed the HSI to rise 1.73 per cent through January, becoming one of the best performing global indices for the period. We expect regulation will continue to have a major influence on the Hong Kong market during 2022 and beyond.

Alongside these trade and regulatory considerations, the spectre of inflation and rising global interest rates are also shaping market performance. Already in 2022, we have seen volatility caused by the forward signalling of tightening US monetary policy on global stock markets. In fact the HSI performance would have been even more impressive in January, gaining more than 6 per cent at one point, but for being reigned back by Federal Reserve rate hike messaging.

Conversely the People's Bank of China is moving in the opposite direction on rates, having lowered key lending rates in December for the first time in nearly two years. This is in reaction to the challenges faced by indebted property developers such as China Evergrande Group, as well as an increase in bad household debts. Consequently, Hong Kong will be sitting in the middle of an interest rate tug of war as the world's number one and two economies seek to keep control of inflation and debt respectively.

Push and pull

We should not ignore that this profusion of macroeconomic forces has taken place against a local Hong Kong backdrop which has been challenging for business for the best part of three years. In 2019, Hong Kong slipped into recession for the first time in a decade as a result of the impact of the trade war and a tougher local business environment. 2020 then brought the arrival of the COVID-19 pandemic, which negatively affected trade through supply chain disruptions and decimated tourism, further straining the local economy. However, by Q1 2021 the city managed to rebound to positive growth after six consecutive quarters of contraction. The financial secretary, Paul Chan, has forecast continued growth in 2022. But with the effects of the pandemic still being felt, this will not be a trouble-free journey.

The push and pull of all of these factors is likely to provide Hong Kong with a significant level of volatility in the coming year, providing ample opportunity for hedge funds and other short side traders to take a view and to engage in short transactions. This, in turn, should drive robust lending activity. It is likely that the rich specials environment that we saw in the second half of 2021 will continue through 2022.

> *"The push and pull of all of these factors is likely to provide Hong Kong with a significant level of volatility in the coming year, providing ample opportunity for hedge funds"*

Of course, trading in Hong Kong-listed Chinese shares is not the only route to long or short exposure to China. The eligibility of securities lending in the China QFII scheme, the potential for further development of the Stock Connect platform and synthetic market access all provide opportunities to lenders that are able to navigate those unique and non-vanilla structures. However, it will still be some time before these platforms are open to the vast majority of beneficial owners who make up the bulk of the global securities finance lending community. 2022 is unlikely to bring any significant shift. The importance of Hong Kong in APAC is clear to see, and it remains a market in which Northern Trust and our clients are well placed to capture multiple opportunities in the future. ■

APAC equity finance revenue: A record breaking year

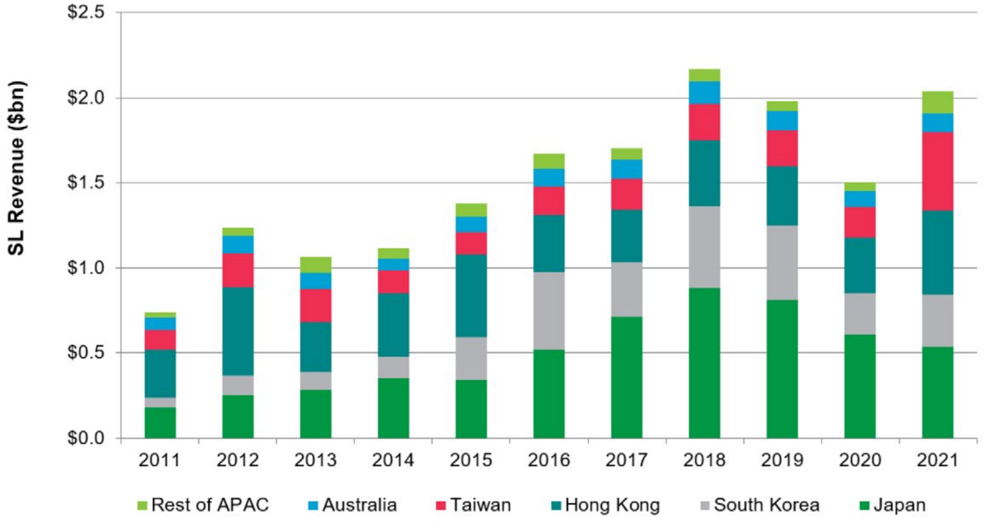
S&P Global's director of securities finance Rob Nunn analyses the resurgence of APAC equity finance revenues during 2021, representing the strongest growth for any regional globally and falling only marginally short of record levels set in 2018

Revenue generated from securities lending totalled US$10.9 billion in 2021, the highest since the financial crisis. This was primarily due to the resurgence in APAC equity finance revenue, which totalled over US$2 billion and fell just short of the region's best year in 2018 (fig 1). The year-on-year increase of 33 per cent was the highest change for any region, driven by the expiry of short sale bans imposed in 2020 as the pandemic eased and concerns in equity markets lifted. This has resulted in an 8 per cent increase in average loan balances and a 24 per cent increase in average fees for the year.

January to June 2021

In the first half of the year, Asia equity lending revenues trended steadily higher from their low point in November 2020, with this trend gaining momentum in the second quarter after the short sale ban in South Korea was

Fig 1: APAC equity finance revenue



Source: IHS Markit Securities Finance

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lifted. During H1 2021, revenues increased by 8.7 per cent YoY to US$880 million. Hong Kong SAR equity finance revenues were the key drivers, producing 8 of the top 10 APAC revenue generators in the first half of the year. Taiwanese equity finance revenues grew steadily, particularly in Q2, as special balances increased. Malaysia equity revenues surged, largely on the back of Top Glove Corporation Bhd, the top revenue generating APAC security in H1. Australian equity revenues totalled US$52 million in H1, a 16 per cent YoY increase.

> *"The short sale ban in South Korea limited lending revenue for the first four months of 2021"*

Revenues were trending upward by the end of Q1, with March delivering what was, at that time, the highest revenue for any month since December 2019. Returns continued to move upwards in Q2, particularly following the end of the short sale ban for most South Korean listed equities. The H1 2021 year-on-year revenue increase was driven by a 3 per cent increase in average fees and a 6 per cent increase in average loan balances. APAC equity special balances averaged just over US$10 billion in this period, an increase of 55 per cent compared with H2 2020 and a 14 per cent YoY increase over H1 2020. Asia equity lendable assets reached an all-time high of US$2.6 trillion, a rise of 40 per cent YoY. Utilisation of lendable assets averaged 4.3 per cent in H1, a decline of 26 per cent YoY.

Malaysian firm Top Glove Corporation generated the highest revenue of any Asian equity, delivering just over US$27 million in the first six months. This stellar return for Top Glove contributed two thirds of the 664 per cent YoY increase in Malaysia's equity finance revenues. The three next highest revenue-generating Malaysian equities delivered just over US$11 million in combined revenue, accounting for nearly all the growth apart from Top Glove.

Japanese equity revenues didn't fare as well in the first half of the year, with a 9 per cent decline compared with H1 2020 representing the worst start to a year since 2016. The revenue shortfall was driven by an 8 per cent YoY decline in average loan balances and a 3 per cent YoY decline in average fees. The top revenue-generating Japanese equity, Anges Inc, delivered US$8.54 million.

Hong Kong SAR equity finance revenues reached US$242 million in the first 6 months, a 44 per cent YoY increase. Hong Kong SAR equity loan balances averaged US$45 billion, a 35 per cent YoY rise, while average fees increased by 8 per cent YoY. The highest revenue-generating equity for the Hong Kong SAR was China Evergrande New Energy Vehicle Group Ltd, with US$18.7 million in revenue. Shares of the electric vehicle manufacturer saw borrow demand rise amid trading volatility, with the share price recording a year-to-date increase of 139 per cent in mid-February before declining to end June down 7 per cent YTD.

The short sale ban in South Korea limited lending revenue for the first four months of 2021, although the lifting of restrictions in May triggered an upswing in financing activity. South Korea equity finance revenues declined by 50 per cent YoY, although revenues increased 5.8 per cent YoY during Q2 following an 81 per cent shortfall in Q1.

Fee spreads continued to decrease globally in the first half of the year, falling 8 per cent YoY, although average fees for Asian equities rose 3 per cent, partly led by the surge of specials balances in the Taiwan and South Korean equities markets.

July to December 2021

During H2 2021, the APAC region delivered the strongest revenue performance of the equities asset class. A 64 per cent YoY rise in APAC equity lending revenues to US$1.1 billion was almost double EMEA equity revenues. This was fuelled particularly by an increase in specials balances, which led to a 49 per cent YoY average fee spread increase. As in the first half of the year, the lifting of short sale bans resulted in a stellar performance for both Taiwan and South Korea equities, while the rest of the region benefited from new opportunities through IPOs and high demand in the technology sector. Krafton Inc, Lg Display Co Ltd and Au Optronics Corp were among the top 10 revenue-generating names, while China Evergrande Group was once again the top earner in the region, contributing US$25.86 million in revenue.

The weighted average fee for Asian equities between July and December was 1.03 per cent and this was the only asset class that demanded an average borrow cost that exceeded 1 per cent. Taiwan became the highest revenue generating market for the first time in our records, with supercharged revenues of US$310 million, a 239 per cent YoY increase. Four of the top 10 revenue generating stocks in the APAC region were listed in Taiwan, reflecting the demand for emerging market specials. The average fee for Taiwan equities was 2.59 per cent, with Au Optronics, Novatek and Innolux each generating more than US$20 million of equity finance revenue in H2 2021.

South Korea was number four on the list, with revenues totaling US$225 million, a 235 per cent YoY increase. The removal of any remaining short selling bans in the region pushed the average loan balance to US$18 billion between July and December, a 119 per cent YoY increase, while fees increased by 55 per cent YoY to reach 2.48 per cent.

Demand did not keep pace with supply in APAC's largest equity market, which saw Japan generate revenues of US$260m and slip to second place below Taiwan in the H2 revenue table. The revenue shortfall was driven by a 9 per cent decline in loan balances and a 14 per cent drop in utilisation compared to the same period in 2020. Singapore equity was the only other market to see equity finance revenues fall in the APAC region.

Overall, it was a great year for APAC equity finance revenue, generating US$2 billion and contributing to making 2021 the best year globally since 2008.

Fig 2: Global securities finance snapshot 2021

Global Securities Finance Snapshot - 2021

Asset Class	Revenue ($M)	Rev YoY %Chg	Avg Balances ($B)	Bal YoY %Chg	Avg Fee	Fee YoY %Chg	Avg Utilization	Util YoY %Chg
All Securities	$10,983	16%	$2,702	28%	0.40%	-8%	6.6%	-5%
All Equity	$8,788	17%	$1,208	26%	0.72%	-6%	3.5%	-15%
Americas Equity	$3,878	1%	$625	35%	0.62%	-23%	2.8%	-15%
Asia Equity	$2,038	33%	$216	8%	0.94%	24%	4.4%	-18%
EMEA Equity	$1,492	5%	$219	12%	0.67%	-6%	4.4%	-21%
ETP	$640	58%	$93	49%	0.68%	8%	12.6%	11%
ADR	$555	135%	$46	70%	1.16%	33%	8.7%	27%
Government Bond	$1,610	8%	$1,232	28%	0.13%	-15%	26.6%	13%
Corporate Bond	$535	24%	$239	34%	0.22%	-7%	4.5%	19%

Note: Includes only transactions with positive fees

Seeking a sustainable future

Sunil Daswani, Standard Chartered Bank's global head of securities lending, speaks to Carmella Haswell about the importance of ESG, how to reach a sustainable future and what's driving demand and supply within the securities lending market

Standard Chartered is among the 17 opening signatories for revised principles released by the Global Principles for Sustainable Securities Lending (Global PSSL) earlier this month. The principles aim to promote and embed environmental, social and governance (ESG) matters and Sustainable Development Goals (SDG) in securities lending activities.

ESG has been a priority within the market for some time now, with a growing number of investors allocating more than 75 per cent of their portfolio to ESG-compliant assets and 37 per cent making a public commitment to align all or part of their portfolio with a 2050 net-zero target, according to a recent BNP Paribas survey. The dynamic that the securities lending world wishes to attain has never been clearer.

Firms across the securities lending industry have launched platforms and technology that strives to achieve an ESG-friendly solution for its clients. For example, Kaizen Reporting released its ESG monitoring tool, ESI Monitor, in September. The tool provides a framework for its clients to measure and manage environmental and social impact, revealing a client demand to reach a greener way of life.

The importance of ESG

Speaking to SFT, Standard Chartered Bank's global head of securities lending, Sunil Daswani, explores the importance of becoming an open signatory for the revised Global PSSL principles.

He says: "ESG has been on the agenda for many years, but there is a recent acceleration across all industries to embed ESG priorities into their business models. We are committed to delivering sustainable banking and the Global Principles for Sustainable Securities Lending will help to support the work we are doing to incorporate ESG into our services, as we align with the priorities of our clients and the communities we operate in."

Despite a number of indices being available to support investment decision-making around ESG, Daswani believes there is a long way to go in establishing a consistent way of measuring and comparing fund performance at an industry level.

He says: "One challenge is that investors have different ESG priorities, some investors will prioritise carbon emissions, while others will look at issues such as energy consumption, pollution, corporate governance, and diversity and inclusion. This creates an enormous demand for a wide range of data, which needs to be monitored and tracked over time.

"However, we are seeing various initiatives emerge to develop ESG measurement and comparison tools, both amongst individual providers and at a wider industry level. One of the most promising of these is the Global PSSL initiative. This aims to create a global ESG market standard for owners, lenders, borrowers and impact creators, such as Standard Chartered."

Reaching sustainability goals

In May 2021, Standard Chartered announced the execution of its first ESG-linked derivative with Trafigura. The transaction involved combining conventional derivatives risk management with sustainability-linked key performance indicators (KPIs) that are linked to reducing greenhouse emissions from owned or controlled sources, and to sustainable sourcing in the base metals business.

The firm also provides a collateral filtering and monitoring service that gives asset managers the assurance that their investors' ESG priorities are reflected through the securities lending process.

Daswani says: "Given that an investor cannot participate in shareholder votes (typically via proxy), when they have lent a security, they may decide to recall a security to allow them to do so. This issue resonates specifically for ESG-driven investment, where institutional shareholders may play an important role in defining a company's ESG strategy.

"Our configurable, automated share recall service enables clients to make informed decisions on whether to recall securities or leave them on loan. This service helps reduce the opportunity cost by limiting the frequency of recall, and the time period for which securities are removed from the lending programme, whilst enabling investors to engage on key strategic issues.”

Demand and supply

The driving factor of demand and supply within the securities lending market is forever changing, especially when impacted by uncertain times, which has been brought by the COVID-19 pandemic. Daswani reveals that a “negative impact” on revenues has resulted from the combination of volatility and economic uncertainty, as loan demands have reduced, with hedge funds deleveraging and short-selling bans in some markets.

He says: “Lenders have generally taken a calm approach to managing risks arising from COVID-19 and adjusted their securities lending programmes accordingly. One big change since the global financial crisis is the increased transparency in securities lending programmes, so beneficial owners have a better understanding of their programme and the risk parameters.

“As we go through 2021, emerging markets continue to be an attractive sector, with relatively low levels of lendable supply and additional operational requirements leading to higher returns for lenders, particularly early market entrants. As we have seen in countries such as South Korea, Taiwan, Malaysia, and more recently, Russia, initial demand often outstrips supply as new markets open up, and we are likely to see the same in the coming year in China, and other newly emerging markets for securities lending.”

A growing market

After just over 12 months as Standard Chartered’s global head for securities lending, Daswani reveals the changes he has seen within the sector during this time and what is driving the company’s development focus.

“Regulators recognise that securities lending has become increasingly integral to financial markets as a source of liquidity and financing as well as efficient price discovery. Their focus now is to promote transparency and alignment between market participants to reduce market risk and increase efficiency,” says Daswani.

He continues: “Data is key to this, as we have seen with the implementation of Securities Financing Transactions Regulation (SFTR) reporting that took effect in 2020. In addition, the Central Securities Depositories Regulation (CSDR), which aims to harmonise timing and standards of conduct in the European securities settlement industry, will also have an impact, but with the implementation delayed to February 2022, the effects are not yet clear.”

Digitisation is also a priority for securities lending markets, which has become key to regulatory and market endeavours to drive standardisation and efficiency, according to Daswani.

He explains: “Securities lending is already advanced in the use of technology, with more than 90 per cent of securities lending trading volume now done through automated lending platforms, a shift that few would have anticipated 20 years ago”.

The common Domain model also appears to be gaining good traction within the industry. ”This is something which Standard Chartered remains committed to supporting as ISLA drives this item on the agenda forward,” says Daswani.

Sunil Daswani
Global head of securities lending
Standard Chartered Bank


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2021 in review: navigating the pandemic

James Er, head of client management, securities lending, HSBC, observes a strengthening of securities lending activity in APAC into 2022 and the emergence of new opportunities in China, the Philippines and other markets

2021 was a challenging year for global markets, with market participants at all levels of the investment chain navigating their way through uncertainty and ever-changing developments related to the COVID-19 pandemic. The securities lending market was no exception, with lenders, borrowers, beneficial owners, regulators and vendors all needing to be resilient and to constantly adapt to this changing environment.

This evolving dynamic presented a number of challenges and opportunities across regions, especially where social and market policies were implemented to varying degrees to tackle and live with the virus. There were a number of positives in APAC, where structurally we saw a lifting, or easing, of short-sell restrictions that helped boost market liquidity and lending returns. While the start of the pandemic saw a number of beneficial owners rationalising lending programme parameters, we also observed a number of those restrictions ease in 2021 as market participants adapted to the new norm, and a number of large new beneficial owners entered the market.

Resilience revenue recovery

Securities lenders were faced with significant asset value declines and structural market restrictions in 2020. However, 2021 largely reversed these restrictions, particularly across Malaysia, Korea and Thailand.

Malaysia was a key differentiator in the first half of 2021 as the regulator put an end to a 9-month long short-sales ban, coinciding with a spike in demand for a number of COVID-related sectors, as market prices diverged from book valuations. Beneficial owners and fund managers who were engaged in this nuanced market benefited from these significant returns. As we move into a post-pandemic recovery, the market continues to present attractive lending yields and scrip discounts.

In South Korea, sentiment was largely positive as the short-selling ban was lifted on 2 May across KOSPI 200 & KOSDAQ 150 securities, bringing balances and revenues quickly back to pre-pandemic levels. The South Korean Financial Services Commission (FSC) also went one step further, committing to opening up the securities lending market to retail investors to participate in short-selling. The positives were also accompanied by market caution, as the South Korean stock exchange (KRX) and FSC increased scrutiny and introduced a number of new rules across the market designed to identify and mitigate potential systemic threats.

In Hong Kong, US sanctions restricted supply in certain securities, while there was also volatility in some sectors including technology, education and properties. In a market where M&A and IPOs traditionally provided rewarding trades for participants, 2021 was challenged with record low corporate activity.

Elsewhere, Taiwan remained another major driver for 2021 returns as the market index reached record highs, but semiconductor supply chains continued to be impacted by the pandemic.

On aggregate, Asian equities generated nearly 28 per cent higher returns for securities lenders in 2021 relative to the year before, according to IHS Markit data.

In the government bond space, sell-off and repricing of the curve into Q4 2021 pushed some issues to trade ‘special’, particularly in Australia. While there was a measure of tightness at year end in the USD/JPY basis, there continues to be an abundance of Japan Government Bonds in the market given their limited usage as Tier 2 high quality liquid assets. Outside of these two major asset classes, there was continued localised demand for Singapore and Hong Kong government bonds for funding and collateral purposes. Other local debt remained structurally hard to mobilise due to restrictive regulations.

There was also increased inventory levels and activity seen in the corporate bond space. The liquidity crunch in the China property sector increased spreads, especially towards H2 2021. Volatility increased with a series of potential defaults and capital raising to meet repayment obligations.

Entrance and re-entrance of new beneficial owners

In general terms, 2021 saw a shift towards wider adoption of securities lending. Following the decisions taken by a few major participants to halt their lending, the industry started to show signs of reversal of this trend throughout last year.

Global lendable assets grew by over 30 per cent in 2021, according to DataLend. While much of this growth was attributable to the rise in valuations across major indices, the industry also saw new lenders entering this space in pursuit of portfolio efficiency management and performance objectives.

In the Asia region, HSBC also observed passive asset managers factoring in securities lending as part of their fund launch considerations. For instance, the first Hang Seng Tech Index ETF in the market adopted securities lending on day one of its launch and last year HSBC partnered with an ETF asset manager to launch the first-of-its-kind securities lending programme for two SGX-listed ETFs in Singapore. These lender-driven initiatives, coupled with signs of regulatory relaxation — including China’s release of new lending rules for Qualified Foreign Institutional Investors (QFII) — have helped to drive greater market liquidity and maturity with respect to lending in the region. Further relaxation of guidelines, such as the quota easing of China’s Qualified Domestic Institutional Investor (QDII) scheme, could open up further opportunities.

During 2021, it was also encouraging to see risk appetite increasing with respect to collateral mandates. There continues to be demand from collateral providers to widen mandates further across ADRs, ETFs and corporate bonds. From an APAC perspective, this extends to foreign investor identification markets such as South Korea, Taiwan and Stock Connect, where the collateral flows and infrastructure fall outside of standard models. The centralisation of balance sheet management at borrower level, including collateral optimisation, has encouraged synergies across regions, benefiting beneficial owners across their global portfolios.

New markets

Progress in opening new Asian lending markets was slower than expected in 2021 as the industry's resources were diverted to managing the pandemic recovery. Nevertheless, key pipelines include China and the Philippines, where the market continues to see positive updates to lending or short-selling guidelines.

The central-counterparty (CCP) lending structure remains a concern for most types of beneficial owners with regard to handling collateral and cost efficiencies. India is an example of where only a CCP model currently exists for facilitating securities lending. This narrows activities to a very specific set of onshore participants, as regulated international funds are unable to participate within the term and collateral models available. Other live markets in Asia, including Singapore and Malaysia, generally have the CCP model coexisting alongside the widely utilised bilateral model, which provides flexibility for market participants to utilise a model appropriate to their needs.

Regulators have taken significant steps to engage the market in efforts to enhance the guidelines and to promote increased activity. For example, the People's Bank of China (PBOC) has released new administrative measures for securities borrowing and lending (SBL) in the China Interbank Bond Market (CIBM) which are expected to come into effect during the second-half of 2022. These changes are eagerly anticipated by all participants, given the rising allocations towards this asset class.

Looking Ahead

After a relatively stable year of returns for participants, 2022 has got off to an indifferent start given the heightened geopolitical risk surrounding the continuing conflict in Ukraine and its implications for the global economy. For the securities lending industry, key developments around regulations and sustainability continue to evolve.

With the go-live of the Central Securities Depositories Regulation (CSDR) in Feb 2022 and the imminent SEC Rule 10c-1 reporting in the US, market participants have found it necessary to redirect resources towards new regulatory initiatives. This could also influence some of the new markets under review in this article to consider introducing transparency reporting requirements and steps to enhance operational efficiency across market participants.

Growing emphasis on sustainability remains an important consideration as lenders and their agents begin to implement their ESG objectives within lending programmes. The ability to combine cutting-edge technology and automation is likely to benefit participants in balancing returns and their sustainability goals.

Despite the evolving landscape globally, and the challenges this presents, Asia remains at the forefront of opportunities for securities lending participants and beneficial owners – with balances growing in existing markets and a pipeline of new supply through new lending markets, asset classes, and local collateral expansion opportunities all driving expectation of continued growth. ■

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(1) Based on CRR-CRD4 rules as reported on June 26, 2013, including the Danish compromise - without phase-in.

Figures as at 31 December 2020

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(1) RBC quarterly results as at January 31, 2022

(2) Standard & Poor’s (AA-) and Moody’s (Aa2) legacy senior long-term debt ratings of Royal Bank of Canada as of February 23, 2022

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