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ISSUE184 22 August 2017

Pension plans file lawsuit against sec lending six

Three US pension plans have accused six of securities lending's biggest banks of blocking the use of nascent platforms and keeping the market for themselves.

The Iowa and Orange County public employees retirement systems, as well as the Sonoma County Employees' Retirement Association, filed an anti-trust class action suit in the US Southern District Court of New York on 16 August and called for treble damages and injunctive relief.

The pension plans alleged that "having formed EquiLend, the prime broker defendants made it clear to market participants that all new entrants into the market would need to go through EquiLend".

Alleged systematic suppression of free market development by the defendants, which include Morgan Stanley, J.P. Morgan, Bank of America, Credit Suisse and UBS, occurred between 2009 and 2016.

According to the complaint, the defendants aimed to maintain high fees for their stock loan services by boycotting start-up lending platforms and urging clients to do the same.

The pension plans' complaint went on: "Recognising the nascent threat posed by all-to-all electronic trading, the prime broker defendants took steps to organise themselves into a working cartel. Their first step was to form a 'dealer consortium' to protect their mutual interests."

One such platform was Quadriserv's Automated Equity Finance Markets, commonly known as AQS, according to the pension plans. EquiLend, which launched in 2002 as a joint venture to provide post-trade and trading services in securities lending, acquired AQS last year for an undisclosed sum.

The pension plans also alleged that the defendants targeted securities lending platform SL-x, which was "forced" to shut down in 2014.

EquiLend, Bank of American, J.P. Morgan and UBS declined to comment.

The other defendants did not immediately respond to requests for comment.

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Clearstream eyes growth

Clearstream is preparing to support China's Bond Connect initiative in order to offer both direct and indirect access to China's fixed income market, as it boosts its securities lending service to allow assets to be accessed from a single pool as part of its migration to the Target2-Securities (T2S) settlement platform.

The Deutsche Börse subsidiary described the inclusion of a selection of mainland China A-shares in benchmark emerging market indices as marking "a new and exciting chapter in the opening of the Chinese market" that would drive a substantial growth in international interest in Chinese equities.

"Mirroring the progress achieved with the Shanghai-Hong Kong Stock Connect in the equity field, the just-launched China Bond Connect represents a major breakthrough in the development of the China bond market. It will start to do for Chinese fixed income what Stock Connect has done for Chinese equities," Clearstream stated.

Clearstream representatives will be present at the Shanghai International Financial Advisory Council being at the end of August.

In its monthly report to clients, Clearstream outlined its ambition to use the event to cement Clearstream's role in supplying its international expertise along the securities value chain as the Chinese market continues to open.

Marc Robert-Nicoud, CEO of Clearstream, said: "Clearstream has been a strong supporter of the liberalisation of the Chinese capital markets ever since it opened its Hong Kong office in 1991."

"Our business is all about enabling investors and issuers to link up globally on the back of an efficient and safe infrastructure. We look very favourably on recent developments as they are in the best interest of all stakeholders Clearstream supports liberalisation of Chinese financial market."

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The offshore renminbi and comparable bonds market is valued at $100 billion, but the onshore bonds market totals as much as $7 trillion to $8 trillion, with less than two percent held by foreign investors via various quota schemes, according to Clearstream.

The Luxembourg-based market infrastructure provider saw its global securities financing activities drop by 16 percent year over year for July.

Outstanding volume fell to €455.3 billion last month from €539.8 billion in 2016.

Earlier in August, Clearstream boosted its securities lending service to allow assets to be accessed from a single pool as part of its migration to the Target2-Securities (T2S) settlement platform.

Users will gain access to Clearstream's international central securities depository (ICSD) and its CSD assets in a single location.

The move promises to overcome collateral fragmentation and maximise the use of customer's assets by automatically allocating them for securities lending.

The improved service comes with the launch of Clearstream's Automated Securities Lending (ASL) principal suite, which is offered under the banner of the OneClearstream offering.

OneClearstream allows customers to access Clearstream Banking Frankfurt as well as Luxembourg as ICSD, and also LuxCSD as the CSD in Luxembourg.

According to Clearstream, ASL principal combines the efficiency of the ASL service with the simplicity and security of a principal structure and Clearstream Banking as sole counterparty.

ASL principal also minimises customer exposure to the upcoming mandatory buy-ins when settlement fails, which will come into force as part of the Central Securities Depositories Regulation. The new connectivity suite includes access to ClearstreamXact.

Helix to offer repo services to Thomson Reuters

Location: New York | Reporter: Drew Nicol

Helix Financial Systems has partnered with Thomson Reuters to offer its customers the resources necessary to grow managed accounts revenue.

HelixREPO is an integrated trading, sales, and operational system for the fixed income repo finance market that will be available to the North American Wealth Management customers of Thomson Reuters.

Todd Berlent, president of Helix Financial Systems, said: "Through this important partnership, Helix's trading applications are providing Thomson Reuters Beta clients the ability to tap into a fully integrated, hosted, and affordable front-to-back office repo and securities lending solution, which enables buy-side firms to manage the full lifecycle of their securities finance transactions, including the management of collateral, counterparty and interest rate risk."

Thomson Reuters Wealth Management signed up Helix alongside two other service providers, FolioDynamix and Vestmark. It now boasts 150 wealth management service providers on its platform.

SEC launches new disclosure forms

New securities lending disclosure forms Forms N-1A, N-3 and N-CSR are now in play for open-end and closed-end funds in the US, as of 1 August.

The new rules require funds to disclose gross and net income from securities lending activities, fees and compensation in total and broken down by enumerated types. A description of the services provided to the fund by the securities lending agent is also required.

Amendments were made to the forms following a lengthy US Securities and Exchange Commission (SEC) consultation.

Forms N-1A and N-3 also require certain disclosures in fund statements of additional information regarding securities lending activities, as well as amendments to Form N-CSR for closed-end funds.

The SEC originally proposed that similar requirements be included in fund financial statements as part of the proposed amendments to Regulation S-X in order to allow investors to better understand the income generated from, as well as the expenses associated with, a fund's securities lending activities.

Some commenters stated that this would yield estimates that may be costly to audit, and that lengthy disclosure concerning securities lending activity in a fund's financial statements could detract from other disclosures.

The SEC acquiesced to the industry's requests for further changes and the final draft included adopting disclosure requirements to the fund registration forms rather than as amendments to Regulation S-X.

Open-end funds with a 31 July fiscal year-end must now utilise the amended forms in its statement of additional information filed on Form N-1A in its 2018 year-end filings.

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NEX Group launches new solution

NEX Group has launched a solution that enables compliance with revisions to the European Market Infrastructure Regulation (EMIR).

The new solution will support the EMIR regulatory technical standards (RTS) rewrite, which was undertaken by the European Securities and Markets Authority (ESMA) last year.

The new rules are due to come into effect on 28 October 2017.

EMIR aims to improve the transparency of the OTC derivatives market and reduce associated risks for clients, such as the mandatory clearing of some asset classes and the attribution of collateral against open positions.

NEX Regulatory Reporting, which currently processes 15 million transactions per day, covers seven million that come under EMIR rules.

With the launch of the EMIR RTS Rewrite solution through its Global Reporting Hub, NEX aims to ensure that clients can upload data in multiple formats with ease before the October implementation.

Collin Coleman, head of regulatory reporting at NEX, said: "The revised rules from ESMA significantly increase the level and complexity of reporting and affect both existing reporting institutions as well as those that haven't yet had to report under EMIR."

"With the rewrite looming, we encourage market participants to ensure they have a solutions provider in place now, to prevent a last minute scramble towards the end of the year."

NEX, meanwhile, achieved a 35 percent increase to its European repo activity in July, which stood at €228 billion last month.

European repo grew from €169.4 billion in July 2016 to €228 billion at the end of July 2017.

NEX also beat its June 2017 EU repo volume by 4 percent, which previously stood at €220 billion.

The group also experienced a 7 percent change in its US market. The figure rose from $212 billion to $225.2 billion from July 2016 to July 2017.

Volume information includes US treasury benchmarks and agencies, as well as off-the-run securities, including treasury bills.

According to NEX, geopolitical events, such as the US presidential election and Brexit result in June last year were the most significant drivers of fixed income trading over the past 12 months.

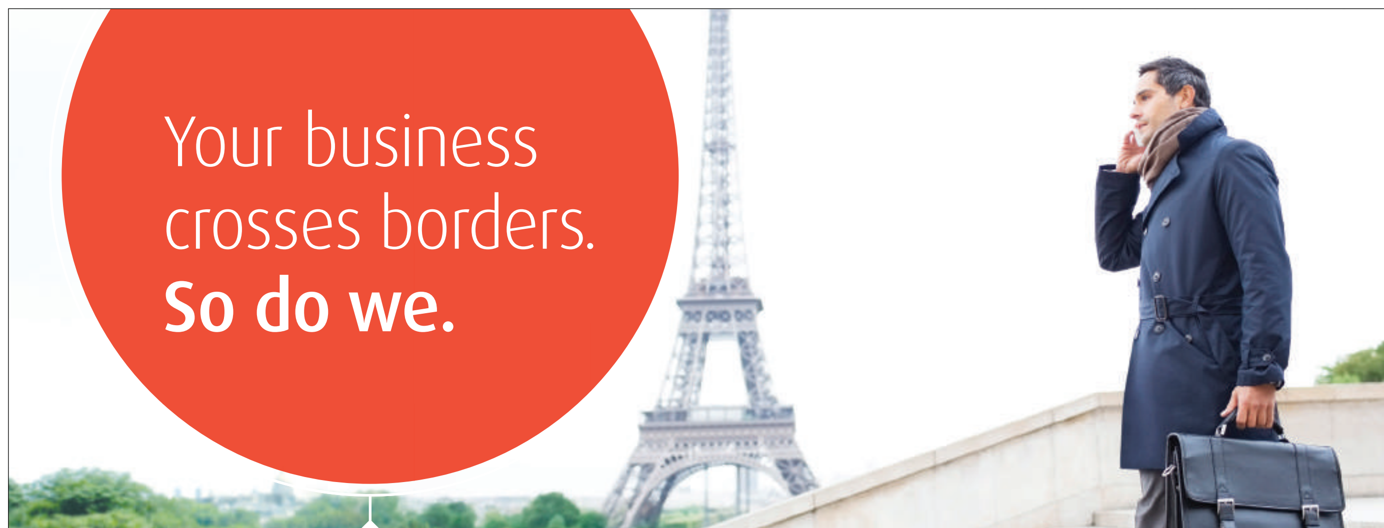
Michael Spencer, CEO of NEX, said: "Our performance remains strong in a tough market environment. NEX Markets has focused on expanding its product suite to a wider client base and continues to win market share in EU repo."

DC Circuit orders capital plan review

The US Court of Appeals for the DC Circuit has called on the US Securities and Exchange Commission (SEC) to reconsider its premature acceptance of OCC's amended capital plan.

The DC Circuit ordered the SEC to re-evaluate OCC's plan due to a lack of effective oversight when originally evaluating its appropriateness in 2015 and 2016.

According to the DC Circuit, the SEC allowed the clearinghouse's capital plan, which has been in place since September 2015 and essentially allows OCC shareholder stock exchanges, including Nasdaq OMX Group and Chicago Board Options Exchange, to swap capital for dividends and refunds, to proceed without demanding adequate evidence and details on certain aspects of the terms.



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Contentious features include an OCC pledge to include independent financial advice when setting dividend levels in order to ensure they are reasonable for the cost and risk associated.

The DC Circuit noted that the SEC failed to verify the appropriateness of OCC's selection of this independent advice. DC Circuit Chief Judge Merrick Garland stated in the court's opinion: "The order's shortcomings are apparent in its discussion of whether the plan pays dividends to shareholder exchanges at a reasonable rate."

"That is a central issue: if the dividend rate represents an unnecessary windfall for shareholders, as petitioners argue, then the plan may run afoul of the Exchange Act's prohibitions by unnecessarily or inappropriately burdening competition, harming the interests of investors and the public, or unfairly discriminating against non-shareholders and clearing members."

Petitioners Miami International Securities Exchange, KCG Holdings and Susquehanna International Group argued that the plan overcompensated shareholder exchanges, which unjustifiably burdens competition.

They unsuccessfully tried to get the DC Circuit to block the plan before implementation began last year. The petitioners further contended that the plan harms investors and the public by transforming OCC from a public utility to a profit-seeking monopoly, and by increasing the fees charged to OCC's customers.

On this point, the DC Circuit added that "only four of nine [OCC] directors representing clearing members voted in favour of the plan, making it less than clear that the process struck an appropriate balance between the interests of shareholders and clearing members".

Chief Judge Garland summarised the DC Circuit's concerns, explaining: "First, the order fails to support its conclusion that the plan's capital target is reasonable."

"Second, the SEC was also too quick to accept OCC's claims that the plan would not increase fees for customers."

"Third, the order fails to give any explanation at all for rejecting one of petitioners' objections."

"Finally, the order gives short shrift to petitioners' objection that OCC, by failing to notify non-shareholder exchanges earlier in its development of the plan, violated its own bylaws."

OCC confirmed that it would provide commissioners and SEC staff with any information it needed to evaluate its capital plan in light of the decision by the DC Circuit to remand it to the agency for further review. Craig Donohue, OCC executive chair and CEO, commented: "While we are disappointed in the court's decision to remand, we are pleased by its ruling that the SEC's order approving the capital plan remains in effect."

"OCC's capital plan is a vital component of our goal of providing world-class service to market participants and helping to ensure the resiliency of a systemically important financial market utility. We intend to submit underlying data and any other information the SEC may request as it further evaluates the capital plan in consideration of the statements made by the DC Circuit in its opinion. We remain confident that the SEC will once again approve the capital plan."

The DC Circuit, with the agreement of the petitioners, has not ordered the capital plan to be unwound, only that the SEC apply a more appropriate level of security to its terms before moving forward. The plan enables OCC to comply with regulatory requirements that ensure a systemically important clearing agency, such as OCC, retains sufficient liquid net assets funded by equity to cover potential general business losses, and also have a plan for raising additional equity if its equity falls close to or below the required amount.

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Whitebox chooses Broadridge

Whitebox Advisors has mandated Broadridge to transform its technology platform into a fully integrated, hedge fund operation.

Broadridge will provide Whitebox with an integrated platform for trading, portfolio management, reference data, reconciliation and data warehouse solutions to manage the multi-billion dollar hedge fund's front-, middle- and back-office operations.

According to Whitebox, this will better enable the hedge fund to respond to new growth opportunities at a quicker pace and increase its focus on core business activities.

Michael McCormick, COO of Whitebox, commented: "Like many funds, we believed that our business was complex and required a very unique set of products and a large amount of customisation."

"What impressed us about the Broadridge product offering was the breadth of the capabilities and their ability to offer it as an integrated solution, freeing us up focus on generating alpha and work that is truly differentiating, by allowing us to simplify our operating environment and reduce our need to be a system/vendor integrator."

LCH launches new SwapClear account

Global clearinghouse LCH has introduced a new type of client account within its SwapClear service that allows buy-side clients to deliver collateral directly and retain beneficial title.

The client account, known as CustodialSeg, promises to increase operational efficiency and eliminate the transit risk arising where a client delivers collateral to the clearinghouse via its clearing member.

LCH noted that segregation at an international central securities depository (ICSD) ensures that such securities collateral remains client specific.

J.P. Morgan is the first clearing member, while Aviva Investors is the first buy-side client, to use this new account type.

BNP Paribas and HSBC have also confirmed their readiness to support the new structure.

To enable a client to transfer collateral directly from its account to LCH, the client or its custodian must open a segregated account with an ICSD.

Euroclear Bank is the first ICSD to provide this service for the CustodialSeg account, which is available for eligible SwapClear clients in the UK, Ireland, Scotland and the Netherlands, which are accessing clearing via a SwapClear clearing member.

Michael Davie, global head of rates at LCH, commented: "As we see a growing number of clients onboarding and actively clearing at LCH, there's increased focus on efficient collateral management."

"We're pleased to bring CustodialSeg to market as part of our ongoing efforts to find innovative ways of supporting the buy and sell side."

Davie added: "The new account structure offers enhanced collateral protection for European clients and simplifies the way they lodge collateral with us."

Barry Hadingham, head of derivatives and counterparty risk at Aviva Investors, commented: "Being able to lodge collateral direct with LCH is a positive step as it allows us to manage our collateral delivery more effectively and to ensure our assets remain identifiable as ours, while lodged at the central counterparty."

"We're proud to be the first client to use this new account type and look forward to continuing this work with LCH."

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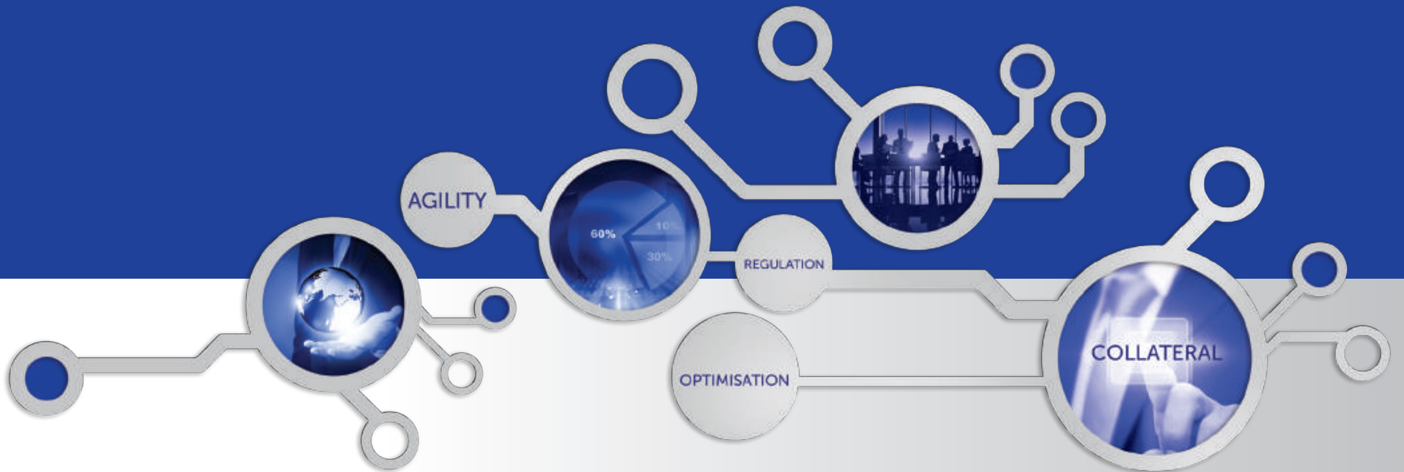

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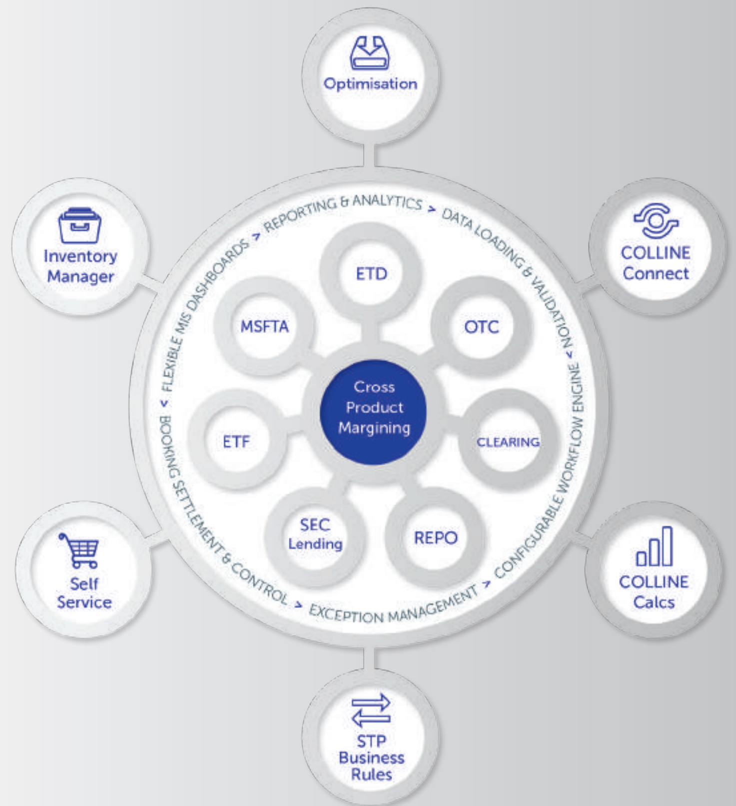

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LCH Group and Euronext secure new 10-year agreement on derivatives clearing

Location: Paris | Reporter: Jenna Lomax

Euronext will sign a derivatives clearing agreement with LCH Group's French arm in Q4 to ensure continuity of clearing services after Brexit and once the second Markets in Financial Instruments Directive II (MiFID II) is finalised.

The agreement allows for clearing services for listed financial and commodity derivatives for the next 10 years between the two companies.

According to LCH, the new agreement will improve value proposition for customers and reduce clearing fees, while also providing continuity of service and economic returns for LCH SA.

LCH SA and Euronext also committed to reducing clearing fees by between 5 percent and 15 percent from January 2019, depending on each specific product and service.

The European stock exchange currently has a 2.3 percent stake in the LCH Group. The exchange will swap this in Q4 for an 11.1 percent minority stake in LCH SA "to allow Euronext to align its shareholdings with its commercial interests in the clearinghouse".

Suneel Bakhshi, CEO of LCH Group, said: "Announcing this agreement is a significant achievement for the LCH Group and highlights the spirit of strong partnership with Euronext."

"We are delighted to be able to offer continuity of services for clearing members and clients while also delivering best in class service and robust risk management across a range of cash and derivatives markets, in line with our open access principles."

Christophe Hemon, CEO of LCH SA, added: "We are delighted to have reached agreement to continue providing clearing services to Euronext and its customers. Euronext's transfer of its shareholding in LCH Group to LCH SA will also further deepen our long-standing relationship."

Canadian and US pension plans enjoy big Q2 returns, say trackers

The RBC Investor & Treasury Services (I&TS) All Plan Universe and the Northern Trust Universe tracker reported fifth and seventh consecutive gains for pension plans in Canada and the US during Q2 2017.

The RBC I&TS All Plan Universe, which currently tracks the performance and asset allocation of more than $650 billion in assets under management across Canadian defined benefit pension plans, reported an increase of 1.4 percent during Q2 2017.

This marking their fifth consecutive quarter of positive returns.

James Rausch, head of client coverage for Canada at RBC I&TS, said: "Canadian pension fund managers have continued to prudently manage portfolio allocations, remaining underweight in Canadian equities compared to domestic fixed income and global equities and generating yet another positive overall return for the quarter."

US institutional pension plan sponsors, meanwhile, notched up investment returns of 3 percent in Q2 2017, according to the Northern Trust Universe tracker.

This marked the seventh consecutive quarter of positive performance for the tracked 300 large US institutional investment plans.

Mark Bovier, North America regional head of investment risk and analytical services at Northern Trust, said: "All plan sponsor segments saw solid performance in the second quarter, and asset allocation played a different role for each type of plan."

"What worked for public funds was a relatively large allocation to non-US equities—16 percent for the median plan, compared to approximately 11 percent for corporate ERISA and foundations and endowments."

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Boeing and JCP name Northern Trust as global custodian

The Boeing Company has mandated Northern Trust to act as global custodian for its €54 billion defined contribution retirement plan, while equities manager JCP Investment Partners has put the bank in charge of its range of Australian fund products.

Northern Trust will provide Boeing's plan with global custody, valuation and unitisation of assets, as well as regulatory and performance reporting solutions, compliance monitoring, derivatives processing and third-party custom cash fund servicing.

Frederick Waddell, CEO of Northern Trust, said of the Boeing mandate: "We are pleased to be selected as a trusted provider that can support all dimensions and directions of Boeing's investment programme."

Waddell explained: "Large, sophisticated retirement plans continue to choose Northern Trust for our unique combination of global scale and highly flexible accounting and reporting solutions that can adapt quickly to changing plan needs. We believe no other provider can offer the commitment to supporting each individual plan's vision better than Northern Trust."

CFTC extends position limit relief

The Commodity Futures Trading Commission (CFTC) will not enforce certain position aggregation requirements until 12 August 2019.

Amended CFTC Regulation 150.4 was due to be enforced from 14 August, but the CFTC extended no-action relief to affected market participants following calls to do so from trade groups and the implementation of US President Donald Trump's de-regulation agenda.

Regulation 150.4, which was amended toward the end of 2016, determines which accounts and positions a person must aggregate for the purpose of determining compliance with the applicable position limit levels.

Exemptions do apply and can be sought, but trade groups including the Securities Industry and Financial Markets Association complained that the requirement to file notices on a prospective basis in search of an exemption would impose significant operational challenges and burdens.

As a result, the CFTC extended no-action relief for affected market participants until 12 August 2019. The delay was originally implemented in February, following Trump's executive order instructing US agencies to cut regulation of financial services.

Specifically, the CFTC will not commence an enforcement action against any person for violating any position aggregation requirement in Regulation 150.4 when they would be otherwise in compliance but for the fact that they do not submit a notice that they are relying on an exemption.

Market participants taking advantage of the no-action relief do have to file a notice within five business days after receiving a request from the CFTC.

First MiFID II limits are set

The European Securities and Markets Authority (ESMA) has published its first three opinions on position limits for commodity derivatives under the second Markets in Financial Instruments Directive (MiFID II).

Proposed position limits on rapeseed, corn and milling wheat set in France are consistent with the objectives established in MiFID II and with the methodology developed for setting those limits, according to ESMA. Limits will apply to the net position that a person can hold in commodity derivative contracts from 3 January 2018.

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GROUPE BPCE

The regulatory years

Were the 10 years that followed the financial crisis a decade of discontent and discomfort, or were the significant regulatory changes necessary? Jenna Lomax takes a look

The day that BNP Paribas closed three of its main hedge funds marked what was the very beginning of the financial crisis. On 9 August 2007, the 10th anniversary of which passed this month, the French bank was forced to acknowledge the sub-prime loan crisis.

It was the first bank to learn the instability of sub-prime mortgage markets, in that it had no way of valuing the assets within them, known as collateralised debt obligations. In the months that followed, a ripple effect would be felt around the world.

The American housing market had lent too much money to people who essentially couldn't afford to pay it back. High delinquency rates led to a slip in value of mortgage-backed securities, which included bundled loan portfolios, derivatives and credit default swaps. The main banks that were invested in these assets—BNP Paribas, Lehman Brothers and the Royal Bank of Scotland (RBS)—began to experience a liquidity crisis. Within a year, Lehman Brothers had filed for bankruptcy, the US government had bailed out Fannie Mae and Freddie Mac, and the investment bank, Bear Stearns, had been bought out by J.P. Morgan.

In the UK, Northern Rock faced a liquidity crisis after borrowing too much money to fund mortgages for customers, which saw the first run on a British bank for 150 years.

Elsewhere, the government had just bailed out RBS for a reported £45 billion. A crisis on this scale had not been seen since the Great Depression of the 1930s.

Although it is clear that securities lending was not a direct cause of the crash, the sector gained a degree of attention in the aftermath because of its loose association with shadow banking. The securities lending market was forever changed by the event because of the regulation that came as a result of it.

Jeff Kidwell, director at Direct Repo, discusses where he was when the financial crisis struck: "I was working as the co-head of the global repo division at primary dealer Cantor Fitzgerald, managing a large repo matched book in New York City."

"At the time, everything escalated very quickly, from rumours about problems with settlements and margin calls, to multiple account portfolio liquidations and massive movement in securities prices," Kidwell says. "We in the industry worked around the clock, frequently past midnight, even on weekends, meeting among our peers and regulators to determine what to do to reduce systemic risk, meeting internally to analyse prices and portfolios and manage various risks, including settlement, possible counterparty defaults, margin calls, and liquidity. The amount of turmoil and upheaval in the repo market (and in broader fixed income and equity markets) were unprecedented."

More than 4,000 miles away in Vienna, Philippe Seyll, CEO of Clearstream, was attending the annual Sibos conference. Looking back, he says: "Most of us senior banking representatives had to leave the conference to go back to our head office to attend crisis meetings."

Andrew Dyson, CEO of ISLA, who was based in London at the time, remembers: "Upon seeing the first signs of the crisis, I was struck by how similar the circumstances were to the UK's secondary banking crises of the mid-1970s when we saw a dramatic crash in British property prices that caused dozens of small ('secondary') lending banks to be threatened with bankruptcy. I thought what was happening all looked very familiar, but the scale of what was now before us was very different."

In the years that followed, sweeping changes were made to how financial services are regulated, as entire economies were bailed out from the brink. In Greece, a furious austerity programme is still being implemented, drawing regular protests from a population that feels like it's being punished for the mistakes of bankers.

Basel III, in particular, was created in response to the perceived lack of regulation prior to the financial crisis. It was introduced in 2010 but is so complicated that it will take until 2019 to implement the regulation in its entirety. Its intention was to strengthen capital and liquidity asset holdings, as well as leverage ratios, essentially to guarantee that financial institutions will have the capital they need should a crisis come calling again.

Seyll says of the sweeping regulatory changes of the last decade: “I believe that good cooperation between the banking sector and regulators is helping the financial market to be operated in a most harmonious manner. I am pleased that the market participants, jointly with the regulators, have undertaken a number of reforms to further strengthen the genes of the financial markets. In my opinion, the groundwork that financial markets are based on is now more solid and elaborate than it used to be.”

But there is a catch, particularly where businesses such as securities lending are concerned. Seyll says: “I feel that in my role as co-CEO of a financial market operator, I am now spending even more time on those topics.”

Andrew Dyson says of new regulations: “The flow of post-crisis regulation has created a more transparent market and specific regulations, such as the Securities Financing Transactions Regulation (SFTR), which will address legacy concerns around transparency.”

“There is no doubt that with banks being better capitalised and adhering to more robust prudential regulation, they should be better positioned to withstand any future market traumas.”

“However and notwithstanding our support for better and more effective regulation, we do see risks primarily associated with the provision of market liquidity as potentially being magnified as a result of some of the current regulatory regimes.”

Kidwell adds: “Depending on which definition of shadow banking you are speaking about and which regulatory reforms combatted it, I’m not sure that all sectors of the market benefited from those rules. I believe that many may have suffered a significant loss of liquidity that has yet to return.”

The next decade

Skip ahead 10 years to 2017 and President Donald Trump is in the White House and de-regulation is top of the agenda. In his first six months as president, Trump signed 38 executive orders, with three eying up a lessening of the regulatory burden placed on banks since the financial crisis struck.

In particular, Trump ordered US agencies to conduct a review of post-financial crisis regulation, with a view to rolling back rules that have adversely affected profitability.

The Treasury has since reported that there is a range of changes that can be made, including substantially amending the controversial Volcker Rule, which restricts short-term proprietary trading using banks’ own funds, and is under threat of being scrapped altogether by the Financial CHOICE Act currently making its way through Congress.

These are just two regulatory overhauls being discussed and are far from the sum of what could be undone under a Trump administration, although, after everything they’ve been through, it would be wise to seek the opinion of financial institutions, from their securities lending desks to their CEOs, to find out what exactly it is they need from a de-regulation programme.

Kidwell says: “With over $30 billion spent by the financial industry so far on the new regulatory reforms and painstakingly managing their firms’ responses to them, I wonder how willing those firms will be to now scrap all of that work and expense to embrace repeal of portions or all of those reforms.”

A decade ago, they started their journey through one massive change. They might not be prepared to embark on another. **SLT**

Financial crisis: How it happened

9 August 2007

BNP Paribas freeze three of its major hedge funds

14 September 2007

Northern Rock faces a liquidity crisis and needs a loan from the UK government after demand for securitised mortgages falls

24 January 2008

Analysts announce the largest single-year drop in US home sales for 25 years

17 February 2008

The UK nationalises Northern Rock after the bank borrows too much money to fund mortgages for customers

14 March 2008

Failing investment bank Bear Stearns is bought by J.P. Morgan

7 September 2008

The US government bails out Fannie Mae and Freddie Mac—two huge firms that had guaranteed thousands of sub-prime mortgages to customers in the US

15 September 2008

The US bank, Lehman Brothers, files for bankruptcy after the sub-prime mortgage market falls into disarray

13 October 2008

To avoid the demise of its banking sector, the UK government bails out several banks, including the Royal Bank of Scotland and Lloyds TSB

2 April 2009

The G20 agrees on a global stimulus package worth $5 trillion

2009 onwards

Basel III is introduced by the G-20’s Basel Committee on Banking Supervision, aiming to strengthen banks’ minimum capital ratios in an effort to prevent another financial crisis from occurring, while major markets around the world embark on the reform of their own financial services markets

10 October 2009

George Papandreou’s socialist government is elected in Greece, marking the start of a fierce austerity programme

2 May 2010

Greece is bailed out by the EU for the first time, with a loan of €110 billion

12 March 2012

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Weathering the storm

The repo market has a chance to sculpt the EU Money Market Fund Regulation to relieve some of the stress that it would put reverse repo under as proposed. Drew Nicol examines the responses to ESMA's consultation

The European repo market is struggling against major market forces beyond its control. The stresses and strains that these are causing are easily observable from both sides of the transactions and multiple industry associations and notable figures have spoken of their deep concern about the market's future.

Repo's woes can be boiled down to a lack of accessible but much coveted high-quality liquid assets (HQLA) to be leveraged as collateral. HQLA has been siphoned off bit by bit by firms to comply with new collateral requirements, while also being hoovered up in significant quantities by central banks as part of their ongoing asset purchase programmes.

Now, however, the EU has a chance to avoid tightening the screws still further if it makes the right choices going into the final phase of its drafting of the money market fund (MMF) reverse repo rules.

The European Securities and Markets Authority (ESMA) has closed its consultation on the first draft of regulatory standards to manage the liquidity and credit quality risks associated with collateral received as part of MMF reverse repo activities. Thirteen industry stakeholders made up of major global banks and industry associations responded, with largely positive feedback on ESMA's proposals.

For the repo world, the incoming MMF Regulation (MMFR) presents an opportunity, rather than another burden to be avoided.

The Irish Funds Industry Association (IFIA) said it best in its response letter to EMSA: "[F]ollowing the implementation of the MMFR, MMFs will become more reliant on short-term reverse repos. This fact underscores the importance of ensuring that the conditions for reverse repos falling under Article 15(6) are appropriately calibrated and future-proofed."

"This is particularly the case in light of the capital conditions being imposed on banks under the fourth Capital Requirements Directive, which mean that banks are increasingly constrained in the level of short-term repo in which they can engage."

As part of ESMA's consultation, stakeholders were offered five options on how best to manage liquidity and credit risk, and the industry was almost totally united in its response.

On liquidity, 10 of the 13 respondents favoured option A, which focused the measurement of risk on the counterparty of the trade, as opposed to the theoretical liquidity of the collateral itself, or piggybacking of other existing regulatory collateral standards.

Two respondents declined to choose a prefered option and one highlighted significant issues with option A and B (the main two choices) without choosing a favourite.

Option A is based on an approach whereby liquidity requirements applying to the collateral depend on the risk of default of the counterparties to the reverse repo agreement and the applicable counterparty risk diversification limit.

Under option A, ESMA stated: "An MMF may only be forced to liquidate those assets following the default of the counterparty to the reverse repurchase transaction. As a consequence, should the risk of default of the counterparty be limited, based on applicable regulation, no specific liquidity requirements may apply, since as long as the counterparty to the MMF does not default, the assets received as collateral shall not and will not be liquidated by the MMF."

"However, when counterparties to the MMF may default, the MMF may be forced to liquidate assets received as collateral. Under such circumstance, the liquidity profile of the MMF may be endangered. To avoid so, additional liquidity requirements shall apply to address that potential risk."

As part of option A's exempted counterparties, ESMA included European credit institutions, investment firms, central banks, and regulated central counterparties (CCPs), among others.

Of the rejected options, Option B focuses on the overall market liquidity value of the assets used as collateral. Option C has an emphasis on using Basel III's HQLA definitions to supplement Option B's framework. Option D has an emphasis on European Market Infrastructure Regulation terminology and Option E offered a variation of Basel III rules.

In its response to ESMA's regulation draft, BlackRock stated: "We note that option A is the most appropriate, and fits with how we would undertake risk management for our reverse repo activity: with risk management (including haircuts) set based on an assessment first of the counterparty, and then the collateral."

"However, it is important to note that repo markets are changing: banks are the main counterparties today, but increasingly, the market may move more towards a less dealer-driven market structure where, for example, MMFs deal directly with insurers or pension funds (who, because of clearing rules, will see an increase in demand for the asset side of repo)."

BlackRock also noted that "other developments could see MMFs looking at direct access to cleared repo (and hence CCPs as counterparties) or indeed, even seeing central banks provide reverse repo facilities (as with the New York Federal Reserve reverse repurchase programme in the US)".

"The rules need to recognise not just what the market looks like today, but allow for how the market is expected to evolve in the near future. The proposed measures recognise CCPs and central banks alongside credit institutions and investment firms. We recommend including insurers and pension funds rather than treating them as 'unregulated' for the purpose of the liquidity assessment criteria."

Given the work that ESMA has put in to shining a spotlight on and limiting this type of alternative financing, commonly known as shadow banking, it's unclear how well suggestions to include pension funds and insurers will be received.

In terms of further credit requirements on reverse repo transactions, BlackRock simply stated that, due to collateral being of HQLA standard, "we [BlackRock] do not believe further prescriptive rules on credit quality are necessary".

Asset management firm Amundi, a subsidiary jointly created by Credit Agricole and Societe Generale, emphasised BlackRock's views. It said: "Amundi clearly supports option A. Option A is intellectually strong and practically efficient."

"First, it rightly considers that the primary risk in a reverse repo lies with the counterparty and that collateral comes only after; as bankers use to say 'good guarantees do not produce good credits'. Option A is correct when it focuses on the capacity for the MMF to enforce its rights in case of default of the counterparty."

BVI, which represents the interests of the German investment fund and asset management industry, reinforced what over-stringent rules could mean for the market.

"Further limitations would prohibit continuing reverse repos as the collateral is very limited. Moreover, reverse repos are an important tool to manage short dated liquidity in the negative interest/excess cash environment."

"Further limitation with regard to credit quality and liquidity requirements would lead to a reduced market capacity for MMFs."

From the point of view of the securities financing market, raising the bar on collateral requirements for MMFs would damage the overall market twice over. First, by potentially bringing down the overall number of transactions being conducted while also tying up yet more HQLA at a time when the EU market is crying out for more high-quality liquidity. On the other hand, an active MMF demographic in reverse repo market could be a boon to the liquidity of the market, much to the relief of all involved. **SLT**

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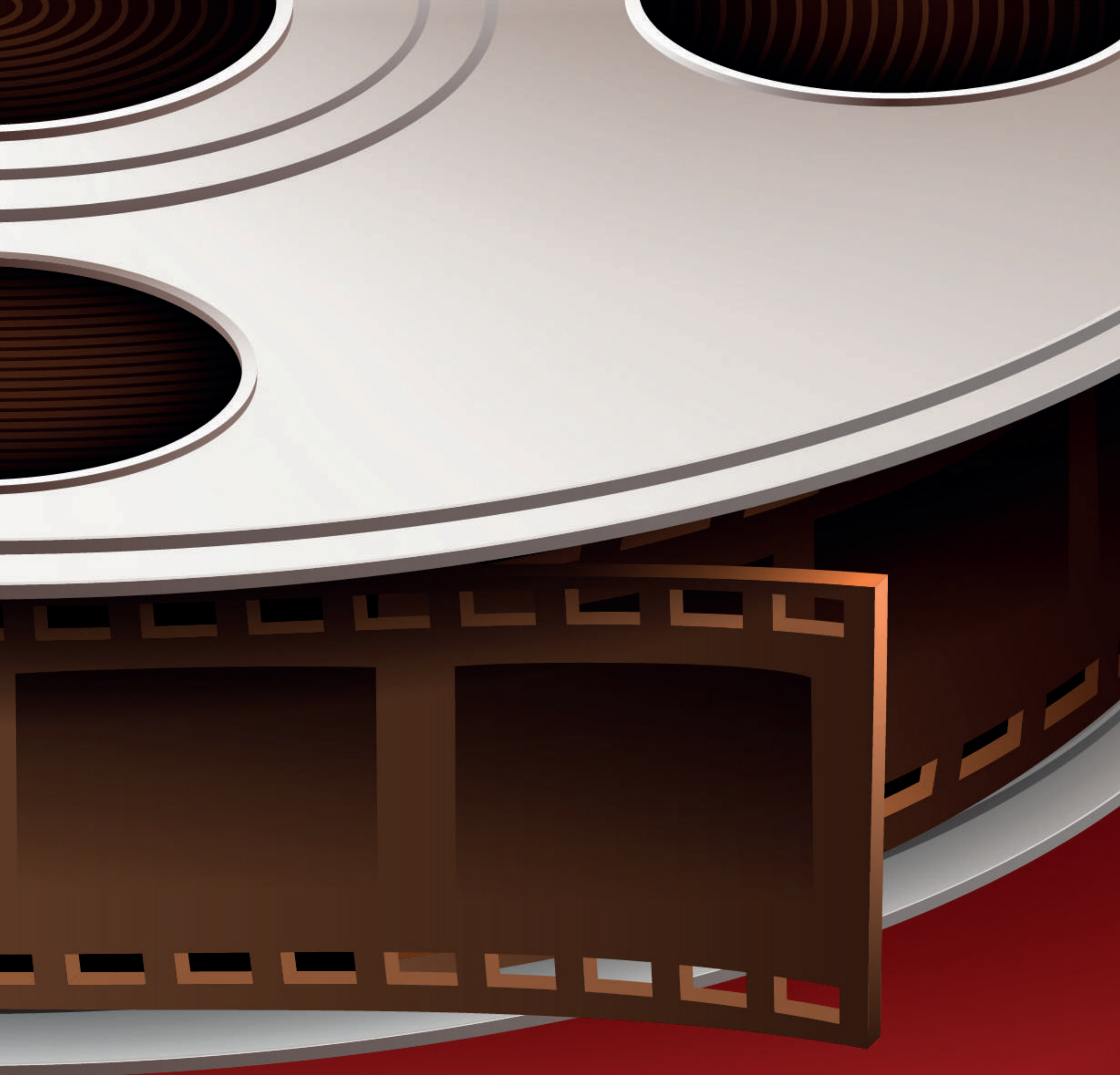


Shorts pile into action-packed cinema stocks

Falling audience figures and online competition is making cinema operators a favourite target for short sellers. IHS Markit's Simon Colvin investigates

Cinema stocks are some of the least rewarding assets to own right now. An increasing number of short sellers are vying to enter this horror show for long investors, and we may be in for Oscar-worthy drama before the final credits. In recent years, digital streaming service providers and the high cost of tickets have cannibalised the market for cinemas.

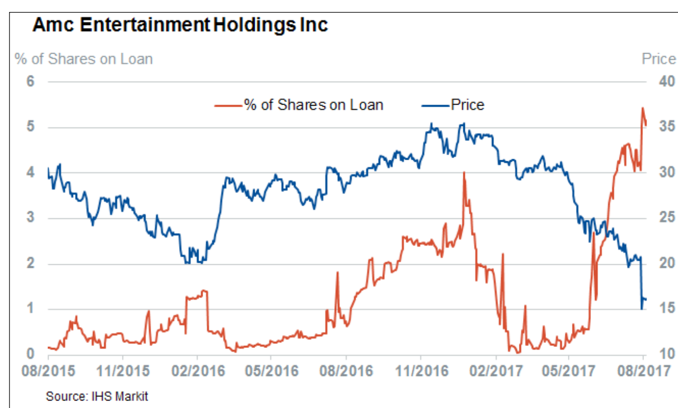
To make matters worse, audiences are increasingly gravitating towards a narrow range of titles, and the industry's fortunes have depended upon high-cost 'blockbusters'. Although the blockbuster strategy worked for a few years, tanking franchises are swelling the ranks of sceptics. The industry's ability to keep drawing audiences—and its wider relevance in a highly competitive landscape—are now under question.

Short sellers circle like Jaws

Short sellers materially increased their positions in all four major North American cinema operators over the past few weeks. These four shares have fallen by an average of 15 percent since the start of the year, and the sector now has an average of 8 percent of shares on loan–the highest in several years.

Regal Entertainment is the biggest target for short sellers. It currently has more than 15 percent of its shares on loan. Interestingly, until now, Regal has performed better than its peers, but short sellers are doubting this resilience. The demand to borrow Regal's shares surged by more than 50 percent in the past three months.

Since the end of May, short interest for AMC Theaters increased more than 15 times. Short sellers were handsomely rewarded when AMC pre-announced disappointing earnings, and on the heels of this news, the company's shares lost more than 25 percent of their value.



AMC technically has 5.6 percent of its shares on loan, but this figure hides the true demand to short the company.

The majority of AMC shares are held by majority shareholder Dalian Wanda Group, which means that the portion of its free float being shorted is nearly three times higher.

With this in mind, AMC is the runner up for the Most Shorted Theater Stock Award.

The other two players in the sector, Cinemark and Cineplex, have also attracted more than their fair share of short interest. Cinemark has 6.7 percent of shares on loan and Cineplex has 4.2 percent of shares on loan.

With the bigger picture in mind, the shorting activity of these four companies underscores the structural challenges faced by the entire sector.

IMAX not targeted by short sellers

The one industry player that hasn't experienced an increase in shorting activity is IMAX. Granted, IMAX has had plenty of operational woes, which bumped off more than a third of its share price in recent months.

Despite its share price plunge, IMAX has not fallen prey to a Zombie Apocalypse by short sellers. The demand to borrow its shares has actually decreased to the lowest level in more than three years.

While IMAX's short interest is technically elevated (7.5 percent of shares are currently out on loan), this figure is notably lower than that of Regal and AMC.

Indeed, the market may be betting on an ever-progressive demand for the unique IMAX entertainment experience. **SLT**

Simon Colvin
Analyst
IHS Markit

> Despite its share price plunge, IMAX has not fallen prey to a Zombie Apocalypse by short sellers. The demand to borrow its shares has actually decreased

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Arrivals and departures at J.P. Morgan, HSBC, Value Partners and more

Paul Wilson has left his role as global head of agent lending product and portfolio advisory at J.P. Morgan Investor Services.

Wilson was global head of agent lending product and portfolio advisory at J.P. Morgan, with responsibility for management and development for the securities lending product.

He was also in charge of defining and managing the business and product strategy, driving and delivering the product development process to improve client satisfaction, reducing risk, and improving operating leverage.

Wilson has been at J.P. Morgan for the better part of 30 years. He has held a variety of different positions within the investor services business at J.P. Morgan, including operations, sales, client management, client service, product development and product management.

Citi's co-head of Americas investor services sales, David Tenney, has left the bank after four years.

Tenney was responsible for leading and managing teams focused on the distribution of prime brokerage, collateral management, delta one, futures, clearing and capital introductions.

In a statement, Tenney confirmed he plans to pursue new opportunities after his 90-day garden leave period ends. It began in July.

Tenney is considering roles on both sides of the investment banking business, including traditional asset managers and hedge funds.

"I am grateful for the opportunity to have worked there for the last four years, which gave me a platform to further hone my technical, leadership and management skills," Tenney said.

"Most importantly, I am grateful for the support that I received from my direct team and the broader equities team—the success we enjoyed in growing the business was the result of a truly collaborative effort that spanned both the prime finance and equities businesses."

Prior to Citi, Tenney was head of client relations at Forester Capital for eight months.

Tenney began his career at Goldman Sachs where he rose up the ranks over 21 years to become co-head of Americas equity research between 2001 and 2007.

He was also COO of global research from 2004 to 2007.

TriOptima COO Mireille Dyrberg is leaving her role in September.

She joined the OTC derivatives markets solution provider in 2008 as CEO of TriOptima in Europe, the Middle East and Africa.

As COO, Dyrberg is responsible for infrastructure functions, including legal, marketing, industry relations, human resources, administration, finance and accounting.

She previously worked at Dresdner Kleinwort.

TriOptima's parent, NEX Group, declined to comment on her departure or a possible replacement.

Organisation CEO Stuart Connolly and Yutaka Imanishi, CEO of the Asia Pacific, remain in their roles at TriOptima.

Karl von Buren has taken on the role of HSBC's global head of prime finance, following the departure of Paul Hamill in July.

Von Buren, who is based in London, was formerly head of equity finance and delta one, having worked his way up the ranks since joining HSBC in 1997.

Hamill vacated the role after nearly six years at the bank and is now on gardening leave.

Von Buren's promotion marks the second senior role change in the bank's prime desk in July after Paul Busby, HSBC's former head of prime finance for the Americas, left to become ENSO's global head of sales.

Mirae Asset Global Investments's head of exchange-trade funds (ETFs), David Quah, has joined asset management firm Value Partners Group.

Quah spent a little over a year at Mirae Asset Global Investments in Hong Kong, where he specialised in ETFs. Before that, he plied his trade at Hong Kong Exchanges and Clearing (HKEX), where he was most recently a vice president in cash trading product development and marketing.

He will co-lead the Value Partners quantitative investment solutions business with Mak Ling Kai, who has overseen the launch of multiple smart beta ETFs in Hong Kong.

Societe Generale has appointed Dereke Seeto as managing director in its Hong Kong office.

Prior to joining Societe Generale, Seeto was Credit Suisse's Asia Pacific head of flow financing within the prime brokerage division, also based in Hong Kong.

The role involved managing the bank's Asia Pacific stock loan desk, as well as futures, swaps and clearing businesses.

Seeto moved to Hong Kong from his role as Credit Suisse's Australian head of prime services in 2011 to replace Neil Hounslow who moved to J.P. Morgan. Seeto was also a member of the board of directors from 2012.

Seeto first joined Credit Suisse in 2000 as part of its prime services trading swaps and stock loan desk.

The California State Teachers' Retirement System's (CalSTRS) deputy chief investment officer (CIO) Michelle Cunningham has retired, having spent 27 years with the pension plan.

Cunningham, who will leave on 31 December, has had an investment career spanning 35 years and was the first internal investment officer to be appointed at CalSTRS in 1991.

At the time of her hiring, CalSTRS's total fund was valued at $35 billion. It now has assets totalling approximately $208.7 billion, as of 30 June 2017.

Promoted to director of fixed income in 1997, Cunningham was responsible for managing several portfolios, including mortgage-backed securities. She was made deputy CIO in 2012.

Christopher Ailman, CIO of CalSTRS, said: "She [Cunningham] is a commanding force to reckon with, this combination of traits defined her leadership style. She's well-respected, and our staff naturally want to do their best for her. She has been instrumental at helping us achieve superior returns."

Allan Emkin, managing director at Pension Consulting Alliance, which acts as general investment consultant to CalSTRS, said: “Michelle Cunningham will not be hard to replace, she will be impossible to replace. Whoever follows in her footsteps may do a great job, but they will never match the constant source of intelligence and friendship we've shared.”

Message Automation has brought on Dean Bruyns to bolster its new Securities Financing Transactions Regulation solution.

Bruyns will report to David Farmery, who is responsible for the firm's business development.

Prior to joining Message Automation, Bruyns served as a broker in securities finance and delta one products at US broker-dealer Louis Capital Markets from November 2015 to September 2016.

Bruyns was also a securities finance trader at MF Global from March 2001 to February 2013.

Message Automation was acquired by Broadridge Financial Solutions in March to bolster its suite of post-trade services.

Citi has hired Mina Kinsey for its equity finance trading desk.

Kinsey joined the bank from EquiLend where she was vice president of sales from February 2016 to July.

Before that, Kinsey was vice president of sales at IHS Markit for just under three years.

Kinsey, who will continue to be based in London, also offers more than 10 years of experience working within collateral management, tax, and sales.

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Head of Network Management, **KBC BANK NV**

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Treasurer, **LIM ADVISORS**

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Sr. Analyst, **MERCER**

Collateral and Securities Lending Manager, **MN**

Executive Director, **MORGAN STANLEY**

Director/Trustee, **NATIONAL GRID UK PENSION SCHEME TRUSTEE LIMITED**

Trustee, **NATIONAL GRID UK PENSION SCHEME TRUSTEE LIMITED**

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