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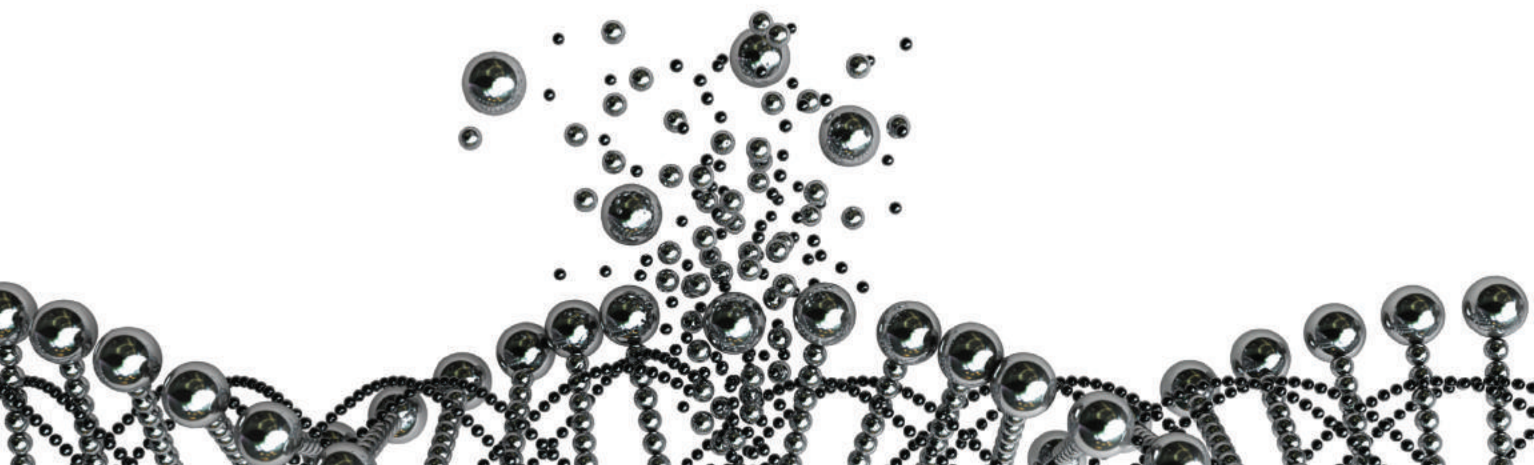

DTCC: the next financial crisis will be different

The next financial crisis will be different, according to a new paper published by The Depository Trust & Clearing Corporation (DTCC).

In the paper, "The Next Crisis will be Different: Opportunities to Continue Enhancing Financial Stability 10 Years after Lehman's Insolvency", DTCC identified a series of actions to tackle new challenges that have emerged related to the macroeconomic environment, market-related risks and the advent of new technologies.

These include expanding central clearing for both cash and derivatives markets to fully take advantage of the risk management benefits provided by central counterparties and boosting regulatory harmonisation and co-operation among all stakeholders to harness the full potential of derivatives trade repositories as early warning signals for systemic risk build-ups.

DTCC also suggests improving risk transparency by globally mandating the use of legal entity identifiers in regulatory reporting and further optimising and accelerating the US equity settlement cycle beyond T+2 to further reduce the exposure associated with unsettled trades.

DTCC further commented that ensuring enterprise data management capabilities become foundational to the risk management framework of financial firms is also crucial, as well as comparing the risk landscape of 10 years ago with today's threats, the DTCC called for a holistic approach to addressing an ever-widening array of interconnected risks.

The DTCC goes on to warn that cybersecurity concerns, while not new, have grown to a point where they may have become the most important near-term threat to financial stability.

Finally, the paper suggests that while fintech developments are not a source of systemic risk at this point, they should be carefully monitored and thoughtfully supervised to balance the associated risks and rewards.

Michael Leibrock, managing director of credit and systemic risk at DTCC, said: "Despite the many enhancements that have been implemented over the past 10 years, the nature of risk has evolved dramatically since 2008."

He added: "Some of the most dangerous and challenging risks we face today were barely registered a decade ago, and the next crisis might be fundamentally different than we can envision right now."

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PGGM: Eurex Clearing is securities lending's 'most important innovation'

PGGM sees Eurex Clearing as the "most important innovation" in securities lending in the past few years, according to Roelof van der Struik, investment manager at PGGM.

He said that the "innovative product needs the backing of committed market parties to make it the success it deserves".

Van der Struik made the comments in a recent interview conducted by Deutsche Börse, in which users of its securities lending central counterparty—PGGM and BNY Mellon—discussed its benefits and industry trends.

According to Van der Struik, "For PGGM, the Eurex cleared lending route complements the current lending routes to market and therefore immediately adds value."

Interviewees were also asked what due diligence measures organisations had undertaken to enable the implementation of central clearing in their business models.

James Day, managing director and business executive for Securities Finance in Europe, the Middle East, and Africa at BNY Mellon, answered: "Clients contract with Eurex Clearing to become a specific lender license holder (SLLH). By becoming an SLLH, they agree and accept the clearing terms and conditions of Eurex Clearing that pertain to securities lending activities."

He added: "As a result, clients' legal and risk teams are fully engaged and are carefully and thoroughly reviewing the clearing terms and conditions to ensure they fully understand all of the rules and nuances associated with the central counterparty (CCP) model."

When asked what recent regulatory requirements had influenced decisions to participate in a cleared solution for securities lending and repo, Day said: "Regulatory factors have been a major force in shaping the securities financing industry over the last several years."

He added: "Clients are aware of the changing environment in which they operate in, and are keen to remain relevant to borrowers and continue to generate revenue from their lending programmes. They are viewing the CCP as one of the tools to enable them to meet that objective."

Higher volatility puts low beta strategies in a sweet spot, says Lyxor

With the US equity market under selling pressure early September, the MSCI World has registered its worst week since late March, down almost 1.5 percent, according to Lyxor's weekly briefing.

This occurred in a context where the probability of an escalation of trade tensions between the US and China has increased, Lyxor said.

The investment company explained: "The deadline to make public comments on $200 billion of proposed US tariffs on China's imports was on 6 September."

Early August, US President Donald Trump signalled the tariffs could be as high as 25 percent. Meanwhile, emerging markets assets continued to sell off.

In the hedge fund space, low beta strategies outperformed last week. Of this, Lyxor said: "Merger arbitrage, which has structurally a low beta versus equity markets, was the sole strategy in positive territory."

It added: "Positive contributors to performance include the Aetna versus CVS deal whose deal spread tightened on the back of media reports suggesting the Department of Justice may approve the deal within the next few weeks."

Meanwhile, commodity trading advisors were flat despite their long US equities positions and fixed income arbitrage was slightly down.

Lyxor reported strategies with a higher market beta, such as long/short (L/S) equity and special situations were down 1.2 percent and 0.8 percent, respectively.

Over the summer, L/S equity funds took more directionality by increasing market-beta. Funds also recently rebuilt their tilt to cyclicals, which was harmful in early September, stated Lyxor.

In terms of investment recommendations, Lyxor said it "maintained an overweight stance on merger arbitrage until now and we reaffirm it".

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REGIS-TR selected by BME Group

REGIS-TR has been chosen as the trade repository (TR) for BME Group, providing a reporting service solution for Securities Finance Transaction Regulation (SFTR) requirements.

SFTR requires EU counterparties to report their securities finance transaction details to a registered trade repository.

REGIS-TR's SFTR reporting solution combines experience as one of the European Market Infrastructure Regulation (EMIR) trade repositories, and the only TR with approval for both EMIR and The Financial Market Infrastructure Act.

The BME Group will now be able to offer a solution enabling customers to meet their reporting obligations in an efficient and cost-effective manner.

David Retana, managing director of REGIS-TR, commented: "We're delighted to be offering our SFTR services to the BME Group."

He added: "This announcement marks the continuation of our close collaboration with the BME Group to alleviate the reporting burden for market participants to the greatest extent possible."

It added: "The strategy appears to be perfectly fit for current market conditions, where downside risks remain elevated amidst high political uncertainty and rich valuations across equity markets. Deal spreads have narrowed lately but the strategy maintains its appeal thanks to its low volatility in returns and low correlation to traditional assets."

"Mergers and acquisitions will probably be softer in Q3 compared to the same quarter in the past two years, but it is still strong in absolute terms."

ESMA issues latest double volume cap data

The European Securities and Markets Authority (ESMA) has updated its public register with the latest set of double volume cap (DVC) data under the second Markets in Financial Instruments Directive (MiFID II).

The recent updates include DVC data and calculations for the period of 1 August 2017 to 31 July 2018, as well as updates to already published DVC periods.

The number of new breaches is 142 to 126 equities for the 8 percent cap, applicable to all trading venues, and 16 equities for the 4 percent cap, that applies to individual trading venues.

Trading under the waivers for all new instruments in breach of the DVC thresholds should be suspended from 12 September 2018 to 11 March 2019.

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Draft technical standards provide no certainty

The Securities Financing Transactions Regulation draft technical standards, as proposed by the European Commission, "will not provide certainty, clarity, predictability and consistency", according to the European Securities and Markets Authority (ESMA).

As a result, ESMA has declined to amend the draft technical standards as proposed by the European Commission, which relate to provisions on the use of legal entity identifiers for branches and unique transaction identifiers for reporting to trade repositories.

ESMA said the technical standards proposed will "hinder the possibility to take into account international developments and reporting standards agreed at the global level and risk timely alignment with international reporting standards".

ESMA stated it would also deviate from, and create an inconsistency with, the currently applicable European Market Infrastructure Regulation reporting standards.

ESMA's regulation requires it to adopt a formal opinion on proposed amendments to its draft technical standards by the European Commission within a six-week period.

The draft technical standards may now be adopted or amended by the commission.

The instruments for which caps already existed from previous periods will continue to be suspended.

ESMA highlighted that some trading venues in the meantime have submitted corrected data that affects past DVC publications.

For a total number of four instruments, this means that previously identified breaches of the 8 percent and 4 percent caps prove to be incorrect. For these instruments, the suspensions of trading under the waivers should be lifted.

As of 7 September, there is a total of 674 instruments suspended.

Suspensions that were expected to be triggered in the past months due to the publication of the DVC results in the files related to the periods 1 January 2017 to 31 December 2017 and 1 February 2017 to 31 January 2018 cannot be lifted anymore.

Mixed results at NEX in August

NEX Group results show that European repo was up 15 percent year-on-year in August, reaching €261.2 billion, against €228 billion in August 2017.

European month on month change was 4 percent—up from $250.3 billion in July.

The results, showing NEX Group's statistics for August, also indicated US repo activity was down 3 percent, hitting US $217.9 billion

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Activist hedge funds among August top performers

Activist funds featured among the top performing hedge funds in August, according to Mark Scott in a post on the eVestment blog, this week.

The latest eVestment hedge fund performance data show that overall industry hedge fund performance in August came in at 0.04 percent. This brought the year-to-date 2018 industry performance to 1.10 percent.

Among primary strategies, event driven-activist funds were among the big winners in August, with performance of 1.93 percent, bringing year-to-date performance to an increase of 2.72 percent.

Scott identified a number of other interesting figures in the August data. Managed futures funds also put up strong returns, an increase of 1.77 percent for the month.

The performance of these funds is, however, still negative for the year at a decrease of 1.83 percent.

Macro funds were the only primary strategy to post negative returns for the month, with performance coming in at minus 0.30 percent, he wrote.

average daily volume (ADV) for the first eight months of this year. This was compared to $225.8 billion in the same period of 2017.

US Treasury ADV was also down 3 percent year-on-year in August, to $127.8 billion, compared with $131.2 billion in August 2017.

NEX has also released its commentary on the EU repo volumes on the BrokerTec platform.

It said: “For most of August the type of activity was similar to July, with an over-riding ‘holiday feel and slower markets’.”

“Volume has started to return to more normal levels in the last 10 days following the UK Bank Holiday and back to those we were seeing in June.”

“EuroGC+ has been very quiet throughout the summer months, although again, picked up slightly in this last week of August. Month end saw no stress volatility in the repo markets, with only a handful of bonds trading truly special.”

“In the wider market, the US/China tariff ‘wars’ continued and Turkey’s economy became a major focus due to problematic politics, big deficits, double digit inflation and newly imposed US sanctions.”

“The lira is down 40 percent versus where it started the year and the European Central Bank was paying close attention to the situation, especially to the European Banks heavily exposed to Turkey.”

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NEX concluded: "None of these scenarios had a significant impact on our repo volumes and the levels being traded."

OneChicago continues to see volumes decrease

OneChicago has registered a trading volume of 423,436 for August 2018, a 66 percent decrease year-over-year.

The decrease marks a trend as OneChicago revealed that its July volume was 378,641, a decrease of 73 percent year-over-year.

This is compared with June, where OneChicago reported a volume of 554,378, a decrease of 77 percent year-over-year.

OneChicago is a Commodity Futures Trading Commission and Securities Exchange Commission regulated exchange offering Single Stock Futures (SSF).

SSF is a delta one product, on approximately 1,800 equities, including American depositary receipts and exchange-traded funds.

KDPW and PKO Bank Polski partner

The Central Securities Depository of Poland (KDPW) and PKO Bank Polski have partnered for a new standard in the issuance and maintenance of legal entity identifier (LEI) codes.

The LEI is a unique global identifier of legal entities operating on financial markets.

Legal entities are required to obtain and use LEIs under European legislation and have been introduced to improve the transparency and safety of financial markets.

PKO Bank Polski is the first bank in Poland to allow clients interested in treasury product transactions to obtain LEI codes from KDPW. KDPW is the only Polish institution accredited to issue LEI codes in the global LEI system. Issuance of LEIs is a part of an integrated portfolio of services offered by KDPW to support the operation and development of the Polish financial market.

KDPW manages a database of over 15,000 LEIs held by companies in Poland and other countries.

Sławomir Panasiuk, vice-president of the KDPW management board, said: "The modification of the LEI documentation and issuance procedures and the initiated partnership with PKO BP open a new chapter in the way LEI codes can be obtained and maintained."

He added: "Direct access to LEIs from the biggest Polish bank facilitates the process for companies and represents one further improvement offered by KDPW in serving the financial market. The solution is open to all entities operating bank accounts or securities

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accounts—banks and brokers who want to be a KDPW LEI service agent.”

Agnieszka Stachnio, treasury product department director of PKO Bank Polski, said: “The launch of the LEI issuance service available in electronic banking and at the bank’s branches is the first solution of its kind in Poland, addressed to all clients willing to trade in Treasury products.”

She added: “The client simply needs to authorise the bank to obtain an LEI for the client from KDPW when signing or annexing the electronic banking master agreement or visiting a branch.”

“There are no other formal requirements and it takes only minutes to obtain the LEI. Importantly, all clients of the bank who actively use treasury products pay no fee for the issuance and subsequent renewal of their LEI.”

OCC reports volume up 10 percent

OCC has reported that total cleared contract volume in August reached 433 million contracts, an increase of 10 percent compared to last year’s August volume of 395 million

OCC also revealed that its year-to-date average daily cleared contract volume is up 19 percent with 20 million contracts, compared to 17 million contracts last year.

Securities lending central counterparty (CCP) and exchange-listed options activity rose, but futures fell. OCC said that securities lending CCP activity was up 17 percent in terms of new loans from August 2017 with 235,780 transactions last month.

Year-to-date stock loan activity increased 21 percent from 2017 with 1.8 million new loan transactions in 2018. The average daily loan value at OCC in August was $160 billion.

Overall exchange-listed options volume reached 426 million contracts in August, up 12 percent from August 2017. Equity options volume reached a total of 384 million contracts, a 17 percent increase from a year earlier.

This includes cleared exchange-traded fund options volume of 145 million contracts last month, down five percent compared to August 2017 volume of 153 million contracts.

Index options volume was down 18 percent with 42 million contracts in August.

The year-to-date average daily volume was up 12 percent from August 2017.

The number of futures cleared by OCC reached 7 million contracts in August, down 50 percent from August 2017. OCC said its year-to-

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date average daily cleared futures volume is 414,516 contracts, 27 percent less than in the same period in 2017.

Cannabis share shorts achieve new high

Short balances in the US/Canada cannabis sector have reached an all-time high, according to a note published by IHS Markit.

Figures produced by the data specialist show that 17 cannabis-related stocks have seen shares short increase since 1 August.

It also showed that there has been a meaningful reduction in some short positions, notably Canopy Growth, a medical marijuana company based in Ohio.

From an investment perspective, the cannabis sector has been on fire of late, noted IHS Markit. There has been an average share price appreciation north of 30 percent since the start of August for US and Canadian stocks with exposure to the sector.

Sam Pierson, director of securities finance at IHS Markit, commented: "Those stocks currently have a market capitalisation of $51 billion, an all-time high, which has increased by a staggering $22 billion since the start of August. The rally in cannabis stocks has been celebrated by those who own the stocks."

He continued: "However, it's been a tough run for short sellers in the sector, who had been reducing exposure to space from $2.15 billion just following the Canadian legalisation vote in mid-June, to $1.5 billion at the end of July."

IHS Markit said the reduction in short balances was partly the result of share price decline, though the average percent of shares short also declined during that period, from a 4 percent peak in mid-May to 2.7 percent at the end of July.

Since then the rally has driven the short balance to a new all-time high on the settlement for 12 September, $2.17 billion.

Pierson identified the largest contributor to the recent increase in market cap as Canopy Growth.

Its shares have nearly doubled following the announcement of a further $5 billion investment by Constellation Brands.

Investors in Constellation Brands itself were less impressed, Pierson noted—its share price declined nearly 10 percent in the days following the announcement, though they have since recovered three-quarters of the initial drop.

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Taking centre stage

Justin Chapman of Northern Trust and Walter Verbeke of Euroclear discuss their views and the hype around crypto custody

Brian Bollen reports

The emergence of crypto custody and the role it might play in the development of cryptocurrencies into mainstream finance is a hot topic in the finance industry. Previously, Securities Lending Times spoke to Lendingblock's Steve Swain and Archax's Graham Rodford on this topic.

Now, Justin Chapman, head of global market advocacy and innovation research at Northern Trust and Walter Verbeke, global head of business model and innovation at Euroclear, take the spotlight to share their thoughts on the subject.

When asked to define crypto custody and to consider how it will differ from traditional custody, Chapman replied: "Crypto custody solution providers are third-party providers of storage and security services for cryptocurrencies. Users are seeking

cryptocurrency custodians to secure them from theft and loss of their digital assets."

He adds: "Cryptocurrencies are stored in 'addresses', which are based on public and private digital key pairs. For most cryptocurrencies, each address is based on a single private key. Anyone who knows the one private key corresponding to a given single-key cryptocurrency address can move those funds. This is extremely important as digital key management is not something most traditional custodians have dealt with, resulting in the need to build the capability to move into this space."

Northern Trust, through its private equity blockchain solution, has been successfully managing digital keys for a couple of years now, he adds.

In February last year, Northern Trust launched what it claims to be the first commercial deployment of blockchain technology for private equity. It also announced that audit firms can now carry out audits of private equity lifecycle events directly from blockchain. Northern Trust has won two US distributed ledger technology (DLT) patents and says its blockchain development is part of a broader digital strategy for asset servicing.

So why does Chapman think crypto custody is important? He explains: "If you look wider than just cryptocurrencies, say to the digitisation of marketplaces, the custody of digital keys will become commonplace. We have had certificated holdings, immobilised then dematerialised. Digital asset issuance is simply the next evolution of our marketplace."

Traditional incumbent providers would be well advised not to rest on their laurels if he is correct in his assessment of the changing industry landscape, he says: "New players are already here."

He adds: "We have crypto exchanges offering custody services right now with most promoting cold-storage type solutions. While this may be suitable for some individual investors, what we see from the institutional area is the need for a truly scalable and secure solution with immediate access."

"Cold-storage options are costly, operationally burdensome with a significant impact on liquidity."

"Digital key retrieval options measured in hours, or in some cases, days, are generally unattractive to institutional investors. We will eventually see traditional custodians moving into this space with immediate access to custody solutions with consolidated client reporting across both traditional and crypto holdings."

"As part of our market advocacy and technology innovation process, we are exploring the potential for safe, secure custody of cryptocurrencies and digital assets. Northern Trust continues to evaluate and advocate strongly for more clarity globally from governments and regulators regarding classification, market practice and taxation of crypto. This is required before we will offer this service," he ends by saying.

Verbeke explains: "There is a lot of hype around this topic and the material volatility in cryptocurrencies is a clear indication that the hype needs some time to settle down."

"While cryptocurrencies such as Bitcoin and Ethereum seem to take centre stage for the moment, there is a much wider crypto world out there, ranging from utility coins to security—and asset-backed cryptos, some of which regulators are already considering as securities. Central securities depositories (CSDs) are assessing which roles

would fit into our natural remit, where our resilient systems could bring genuine value.

He views initial coin offerings (ICOs) as an interesting evolution. They provide access to liquidity to small- and medium-sized enterprises (SMEs) who would generally not list on an exchange, nor issue fixed income. An ICO issuance cost of $150,000 is significantly lower than the cost of a traditional initial public offering (IPO), but as the quality of the ICO material increases, so will the cost, he adds.

If such ICOs become one of the ways to bring oil into the liquidity machine, in particular for SMEs which are the foundation of the so-called 'real economy', then I believe CSDs should see where and how we can support cryptos and their ecosystems

He observes: "Regulators such as the Autorité des Marchés Financiers (AMF) in France are already offering a kind of quality label."

Verbeke adds: "If such ICOs become one of the ways to bring oil into the liquidity machine, in particular for SMEs which are the foundation of the so-called 'real economy', then I believe CSDs should see where and how we can support cryptos and their ecosystems."

"Not surprisingly, our clients—the brokers, custodians, and agents—are asking Euroclear to look into whether we could take up a role in order to inject our robustness, resilience and reliability into the new crypto ecosystem," he says.

"They want the security we bring. At this stage, we at Euroclear are assessing the new crypto dynamic by engaging actively in the industry and in the regulatory dialogue, and by putting use-cases in place—to help us understand where we could bring genuine value in line with our core DNA."

On risk mitigation, he states that when asset managers and funds invest in capital markets they face not only investment risks, but also many other types of risk, including legal risk, settlement risk, liquidity risk, counterparty risk and others.

There is no reason why that would be different for cryptos.

"Over the years, the capital markets have put pieces of infrastructure in place such as stock exchanges, CCPs and CSDs to mitigate these risks and to bring resilience, robustness, efficiency and security into the markets," he goes on.

"Some of those roles and pieces of infrastructure will certainly also need to put be in place in the crypto world to ensure the same level of security—allowing asset managers and funds to invest in cryptos in a business-as-usual way through their brokers and custodians, and for regulators to feel just as comfortable."

Turning to governance, he begins by noting that most cryptocurrencies are issued in a DLT blockchain environment, which adds complexity and also unfamiliarity to the equation.

The distributed nature of such environments makes it critically important that the right governance and operating models are put in place, he says.

"These are the kinds of things clients can currently take for granted in the securities settlement business," he adds.

"CSDs ensure cash in transactions, settlement finality, and well-managed liquidity. The DLT and crypto world has not yet found similarly robust and resilient solutions."

Constructive dialogue between stakeholders is needed, he states. "I find it quite remarkable to see how key stakeholders look and act in cryptocurrencies."

"I see conversations going on among different CSDs to decide which roles would make the most sense for them to take up."

"I also see a very constructive and collaborative dialogue between regulators, financial market infrastructures and the broader industry with regulatory sandboxes being created as safe testing environments."

"This constructive dialogue is refreshing and powerful. Of course, our clients want the Euroclear group to be an engaged, active partner in that dialogue and that journey, and to contribute to creating a stable and robust environment for the crypto world." **SLT**

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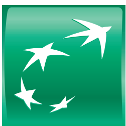

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An emerging market with a promise

IBM and Santiago's Exchange are Chile's biggest securities lending hubs, showing signs of growth, receiving high revenues in one hand, and embracing technology with the other

Jenna Lomax reports

The Bolsa de Comercio de Santiago and IBM have been working together for around 20 years and are the main financial hubs in Chile, currently.

Chile's securities lending model is only utilised to cover fails or facilitate short selling of equities. While short selling is permitted, this is only via an authorised local broker-dealer. Fail coverage can be executed by the Bolsa de Comercio de Santiago—Chile's dominant stock exchange.

But Latin America is an emerging market and change is coming to the region. Chile's Santiago Exchange, the largest exchange in the country, recently announced a partnership with IBM to introduce blockchain technology across the country's financial sector.

The agreement makes the Santiago Exchange the first stock market in Latin America to apply IBM Blockchain technology within its short-selling system for securities lending.

Built by IBM and Chile's Santiago Exchange, the solution is designed to help reduce errors, possible fraud, and processing time for each transaction, while also improving transaction management and lowering costs.

But despite this promising element, Chilean equities are underperforming after a stellar 2017.

In a blog written by Brown Brother Harriman it was stated that in 2017, MSCI for Chile was up 39 percent versus 34 percent for MSCI emerging markets.

So far this year, MSCI revenue for Chile is minus 14 percent year-to-date and compares to minus 9 percent YTD for MSCI emerging markets.

Looking at the numbers

DataLend has reported, as of 30 August, average daily on-loan balance thus far for 2018 stands at $696.64 million on loan/day, with equities standing at $12.26 million and fixed income at $684.38 million. The average daily lendable balance thus far for 2018 is $12.84 billion in lendable per day, while equities are

currently $550.83 million and fixed income stands at $12.29 billion. DataLend found some 56.6 percent of the on-loan balance for Chilean assets is booked versus cash collateral, while the remaining 43.4 percent is booked against non-cash collateral.

Chile is a fairly thinly traded market, according to DataLend, with approximately 125 securities on loan on any given day, almost all of which are fixed income.

DataLend comments that these securities on loan consist of "a mix of corporate, agency and sovereign bonds".

DataLend states: "it is important to note that the fixed income activity seen in Chile is likely to be traded out of The Depository Trust Company or Euroclear, not domestically."

The average utilisation for the Chilean market is 5.42 percent so far in 2018.

Thinking outside the box

As it stands, Mexico is the second largest market in Latin America, with Brazil being the largest.

Mexico and Brazil are the only markets in Latin America to currently count for equity finance.

Mexico has had a securities lending market since the 1990's. Regulation in the jurisdiction meets international standards and there are currently a couple of ways to access the market—local bilateral agreements and electronic platforms with authorisation from the Comisión Nacional Bancaria y de Valores—an independent agency.

In addition, there are two authorised platforms for securities lending—VALPRE and MEIPresval.

Brazil's first securities lending association was launched in August 2013. It is charged with improving communication between international players, local participants and the exchange, which oversees transactions through a central counterparty model.

In Colombia, securities lending is utilised to cover fails or facilitate short selling legal framework which is regulated by Bolsa de Valores de Colombia, the Office of the Financial Superintendent of Colombia and the Securities Market Self Regulator.

Argentina's securities lending framework is largely based on the Brazilian model. Having spent the last few decades under the strict control of the local regulatory authority, the country's financial market is gradually getting freed and its regulator is on the verge of granting permission for short selling.

Though facing current high inflation and the generally weak peso, the future remains unclear for now, while Argentina's National Securities Commission still remains cautious on short selling and it intends to limit this negative impact.

But to add to the uncertainty, Argentina's central bank is said to be discussing a repo loan of as much as $5 billion with foreign banks.

With the aforementioned models in mind, Federico Ortega Gilly of Mexico's Nacional Financiera, explains: "Our efforts as a region should be towards creating a Latin American association for securities lending, similar to the Pan Asian Securities Lending Association."

He adds: "Independently, other South American countries are starting to dig into securities lending markets, they want to settle—the cards are in place to make things good in Mexico." **SLT**

The granular detail

Seb Malik of Market FinReg discusses what was heard at the SFTR London Conference on 5 September

On 5 September in Canary Wharf, Market FinReg convened the largest dedicated Securities Financing Transaction Regulation (SFTR) conference held to date. Delegates attended from both end-user firms as well as the full spectrum of solution providers ranging from legal services and training, data vendors, industry bodies, and trade repositories (TRs).

One speaker, who regularly attends and speaks at industry events, said it was "refreshing to see so many new faces, not just the usual crowd".

The conference might never have happened had we accepted conventional wisdom.

When we floated the idea to convene an international conference dedicated solely on SFTR, we were cautioned with one of the largest SFTR players telling us it wasn't going to work. We needed to broaden the scope, water down the content, discuss collateral, and slip in a few talks on SFTR here and there in order to secure attendance and sponsors.

But securing sponsors, while desirable, was not our primary objective, because with sponsorships come demands for control over the agenda.

We have made no secret of our concern that for far too long the industry has been beset by generic high-level chatter that fails to address the granular details. I believe this failure to address SFTR head-on is not by coincidence.

SFTR is extremely complex and many firms are grappling to decipher the complicated reporting regime. It's something of a white elephant in the room. We all know it, but no one is prepared to say it.

SFTR is the most arduous and complex reporting regime to affect the securities financing business. Comprising four tables, six reports, ten action types, trade, position level reporting, and with only certain valid permutations of the sheer level of detail, has left many market participants confused.

Other participants are reluctant to offer opinions lest they be wrong. We have been privately approached by a number of firms who are leading actors in SFTR, seeking guidance and help in deciphering the complex legislation. In direct response to private requests, Market FinReg convened the International SFTR Conference and billed it "the granular details". This would be an unconventional conference.

We set about to tackle the reporting regime head-on, no holds barred. Delegates were free to interject with open questions.

Mindful of the advice we had received, we were delighted to see the venue packed to the brim in the morning with delegates flying in from as far as the Czech Republic, Germany, India, Ireland and Norway.

The first takeaway gleaned is that there is a genuine thirst for granular details. The industry is demanding more from participants than generic talks on the importance of legal entity identifiers; establishing operating models; project plans; breaking down silos and not leaving it to the last minute. While all valid observations, such high-level topics are fundamentally deficient in preparing the industry for the reporting regime.

We set out to answer the following questions:

- What is the backdrop to SFTR and what is it trying to achieve?
- What data do I need?
- What are the problematic fields?
- How do I transaction report?
- How often?
- To whom?
- What triggers a reporting obligation? What is not a trigger?
- What does a transaction report look like?
- Which fields do I need to complete?
- Do we report all four tables, 10 action types?
- How do we agree on and generate a unique trade identifier (UTI) in time?
- Can you run through examples of real-life transaction reports?

The conference commenced with an introductory talk in which I highlighted Market FinReg's advocacy work in the form of taking legal action against European Securities and Markets Authority (ESMA) and separately the European Commission for their failings under EU law, which were harming the industry. Market FinReg approached banks who shared their concerns but were understandably reluctant to commence action against the regulator to whom they are ultimately accountable.

As for ESMA, we took legal action to oblige it to release the field validation rules which resulted in hundreds of vendors and solution providers building out their products months (years?) ahead of time. One appreciative firm noted: "But at least these firms will have more of a head start thanks to [Market FinReg] … whom we can all thank for making these validations publicly available so early in the cycle. We salute Seb Malik for his swashbuckling endeavour to get this document into the public domain."

After a useful introductory overview by Jonathan Lee of Kaizen Reporting, I presented a series of talks on who is caught by SFTR, extraterritoriality, who should not report, reporting exceptions, report by when and to whom, what are reportable transactions and what are not, and triggers for a report and quizzes to cement knowledge. Subtle details were brought out that may have been missed by the industry such as the view that financial counterparties have to report on behalf of all non-financial counterparties.

Delegates regularly interjected with questions ranging from "what is the definition of employee?", to a question on how to report collateral and liquidity swaps. Delegates appreciated the time and latitude afforded in being allowed to interrupt to ask ad hoc questions.

There was consensus from both Lee and myself that the EU had gold-plated its Financial Stability Board (FSB) commitments by demanding daily transaction reporting on a trade level. Practitioners interested in detailed background reading were referred to the FSB's guidelines.

After the mid-morning break, I explained the concept of trade and position level reporting, and the format of the report. Duncan Carpenter from Pirum then took the stage to explain UTI format and generation responsibilities. This led organically into the first panel

discussion of the day where I peppered Carpenter and Lee with issues surrounding sharing of UTIs between two counterparties and the greater question of pre-trade matching in order to correctly assign UTIs.

Perhaps the greatest takeaway was the necessity for interoperability between vendor providers in sharing UTIs in the event that two counterparties use different data vendors. Carpenter explained that this was very much an open question with discussions ongoing.

The conclusion of the panel discussion led me back to discuss four tables; six reports; 10 action types and their interplay.

And then came the greatest risk for the day. I projected the Excel Field Validation Specification document onto the screens and began to analyse the issues surrounding each of the 153 fields in turn.

I demonstrated how to use the Excel sheet, how to filter for the relevant fields while reporting and highlighted areas of concern that may arise from a particular validation rule.

One participant remarked that we “were stark raving bonkers” for attempting to pull off something so audacious in a conference that contained CEOs, heads of Trading Desks, and managing directors, but that “it turned out to be an inspired move”.

As the conference was billed as covering the granular details, the field by field was essential. I was anticipating half the delegates to break off during my field by field analysis so was pleasantly surprised when all remained.

The next talk delivered by Jo Hide from Regis-TR was perhaps the most flowing and well-delivered talk of all. Hide commanded the room as she walked delegates through their relationship with a TR, what to ask, expect and demand.

Chad Guissani from Standard Chartered moderated the next panel discussion, probing David Masters of Societe Generale, Matt Smith of SteelEye, Hide, and Lee on data issues and lessons learned from previous reporting regimes.

I then ran through four examples of how to report various reporting scenarios ranging from the simplest bilateral repo, to centrally cleared repos each with counterparty facing off to its own clearing member.

Michael Cyrus, head of collateral trading and FX from Deka Bank and Thomas Hansen head of collateral trading from Credit-Suisse joined me on the panel to discuss collateral, collateral reuse and SFTR, collateral scarcity, settlement and the viability of T+1.

Cyrus expressed a view that the European Commission had exaggerated the level of interconnectedness and systemic risk posed by the shadow banking sector. He stated that the EU tended to approach regulation in the wrong way, deciding on what they intended to do, then rationalising it rather than approaching the issue from principles, then data and then regulation when necessary.

This led to the final talk of the day by Cyrus on the future of regulation and the concept of Smart Regulation. He advanced a powerful argument that there is considerable overlap and redundancy in the various reporting regimes which should be corrected.

Our parting advice to participants are twofold. Firstly, to commence by gaining a thorough understanding of SFTR and its obligations via training of all key personal, and secondly to engage in a robust procurement process when selecting data vendors and TRs. **SLT**

As the conference was billed as covering the granular details, the field by field was essential

Seb Malik
Head of financial law (regulation)
Market FinReg

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SFTR, Brexit, and technology reign at IMN

As the securities lending industry descended on London for two days of insight and discussion at this year's annual European Securities Finance and Collateral Management Conference, SFTR remained at the forefront of attendees' minds

Jenna Lomax reports

At this year's annual European Securities Finance and Collateral Management Conference, the Securities Finance Transaction Regulation (SFTR) was mentioned in most panels, while Brexit, technology disruption, and opportunities of pledge were also hot talking points.

In the first panel, the speakers hit the ground running by agreeing and predicting that the SFTR was going to drive the market for the rest of this year.

During the panel, speakers agreed that providing data and delivering data for counterparties will drive where business goes, and as a reporting obligation, while SFTR isn't meant to change market practices, it will.

One panellist warned: "If you're not at a point where you can transmit and reconcile the data [for SFTR], you will not be a participant in the market."

One panellist said: "Borrowers will be very dependent on the lenders for that data. If they can't get the data in the right format, they will have to move the business. The regulation is very complicated. SFTR is definitely going to drive business."

Another panellist affirmed: "We have our best people on the industry working on this. We will resolve it as a regulatory issue. Clients should not be impacted by it. Like every other piece of regulation, we have to deal with it and get through it. We're already putting our best people on it, and generally, the data vendors are participating. They are doing a good job on that, but it is our job to fix it."

Also discussed was the impact of Brexit and what it could mean for the securities lending market.

One panellist said: "I don't think Brexit is an opportunity, it's a disappointing outcome. It's a distraction and a disruption, something that you have to commit resources towards."

Another panellist, giving a US perspective, said: "I think when we talk about regulation and Brexit, it's all about resource distraction and documentation distraction. That's always a challenge. But as with all regulatory issues, the industry has ways to get through them."

Brexit was also discussed in a separate panel on macroeconomic factors and their implications for the European securities finance market.

One panellist asked another whether the "noise" being made about Brexit in the UK was reflected across the EU, or if it wasn't that big of an issue for Europeans.

In response, the panellist said that those in the EU needed to ensure that the wheat was separated from the chaff when it comes to Brexit. The panellist explained that those in the EU are "aware of the key decisions", but try to avoid the politics of Brexit.

"Most investors can handle it, we've got to remain stable," the panellist added.

Another panellist, who said he was speaking from the broker community, said that Brexit is a "multidimensional issue which spans pretty much everything we touch on a day-to-day basis".

"There are the political angles to it, which we are all watching every day. It's very hard to pick the middle ground."

"From our point of view, we are asking clients to come to the table, some of us are hoping some of this will go away, but the reality is we need to plan for Brexit in March. The more effort we can put into that, the better given the timing."

"There's a massive amount to be done in a short amount of time. We want to be ready ahead of March. There's a risk of a lack of awareness at a regulatory level of the critical importance of securities lending and repo in the continued functioning of the market."

During another session, concentrating on critical issues heading the agendas of beneficial owners, the panellist questioned whether lenders struggle to keep up with their clients.

"Do securities lenders live by a vanilla-type business report?", questioned one panellist. The panellist challenged the lenders on the panel suggesting "the minute a client wants to step outside that norm, some of you struggle to keep up with that client".

In answer to this comment, one panellist said: "There has been a legacy thought process in this business to standardise and push that standardisation through. There's increasing agility in providers and across providers. We have the infrastructure, so we're increasingly seeing clients coming to us around initial margin, where they need to generate cash on short notice."

The panellist explained that one reason for this aforementioned struggle to "keep up with the client", might be the increasing level of regulatory compliance, as well as the need to keep up with the speed of technological innovation.

They added: "There's so much going on with emerging technology now, we're spending a huge amount of time around innovation. We're looking at a lot of technology solutions for things like peer-to-peer lending."

One panellist compared the level of innovation available before the financial crisis to now, stating: "In terms of innovation, [in the context of] the financial crisis 10 years ago, lending programmes, across the board, then and now, are hugely different."

Another said: "Times have changed–we understand a borrower's perspective more now than perhaps we may have 20 to 30 years ago." In the same panel discussion, another topic discussed was the consideration of pledge becoming an increasingly viable alternative to market.

The panellist said although the economics might stack up staying where you are, "it does make sense to look at alternatives, and sovereign or state type entities are more likely to want that".

One panellist agreed, but added: "Pledge has been designed by borrowers, but beneficial owners want to commit to certain transaction types."

In a separate panel, which looked at evaluating collateral management and optimisation strategies in today's market, a panellist discussed the recent implementation of phase three of initial margin (IM) requirements for non-centrally cleared derivatives, which formally began on 1 September.

This continues a long-term process launched in response to the global financial crisis of 2008 to 2009, when the G20 agreed to a financial regulatory reform agenda covering the over-the-counter derivatives markets and market participants.

The panellist said phases four and five will have a major impact on the way banks are organised to understand collateral. One panellist affirmed: "We see more collateral post-global financial crisis. The overall trend is toward collateralisation–whether in derivatives forms or pledge forms of collateralisation, these days it's almost moving in real time."

However, when discussing exchange-traded funds (ETFs), one panellist said these type of funds are not ready to be eligible for collateral.

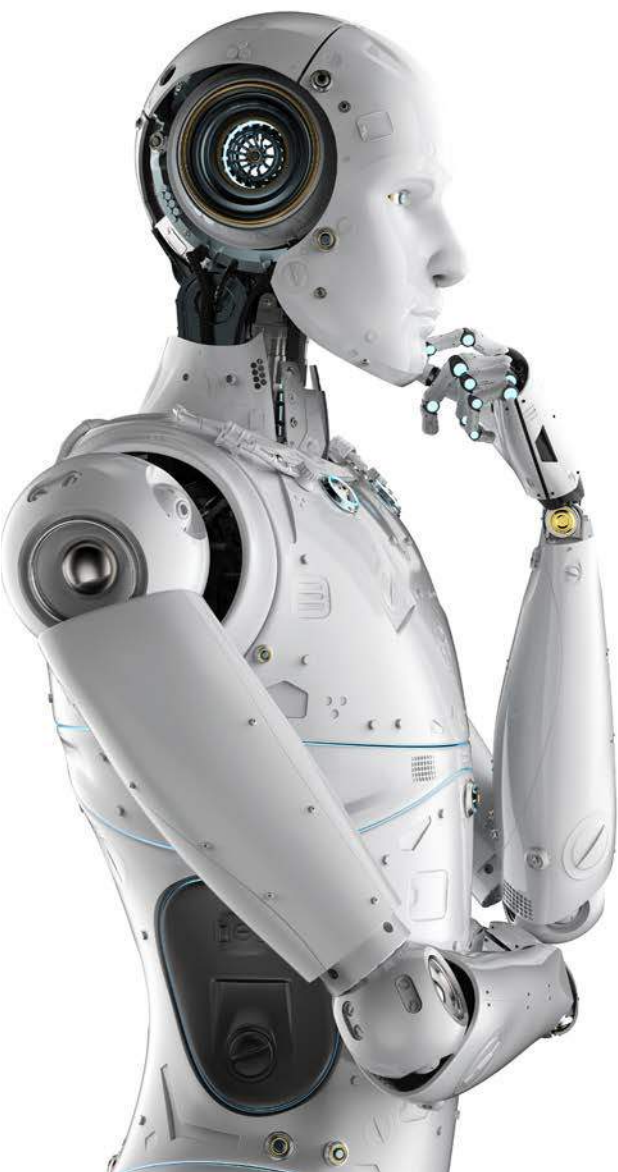
They said: "ETFs, in a lot of cases, are not eligible for collateral, they're not available, or not worth it, you have to consider practical operational considerations."

They added: "From a regulator's perspective, there is still some way to go to make ETFs appeal as an asset class of their own."

On the occasion of the 10th anniversary of the financial crisis, one panellist asked, as the financial market stands, could the financial crisis happen again today, and would it be repeated or avoided.

One panellist stated: "It should not happen again, we are more organised."

Another panellist concluded: "The past shows it's clear what happens in a crisis situation that puts stress on the market, now we have a much greater level of transparency." **SLT**



Technological advance:

opportunities or threats?

David Lewis of FIS discusses how the four 'superpowers' of technology will drive and shape our world going forward

Technology is here to make our lives easier and our businesses more efficient. According to some, there are four 'superpowers' of technology that will drive and shape our world going forward: the cloud, mobile devices, connected gadgets and artificial intelligence. Individually and respectively, they change the way we use or purchase computing power, stay connected wherever we are, leave mundane tasks to machines and even make basic decisions on their own. Combined, they can deliver services and capabilities not yet dreamed of. A recent article observed that supercomputers buried deep in frozen areas of the world, allowing quantum computing theories which need super cooling to become reality, will address mathematical and data problems we haven't yet thought of, such as real-time monitoring of biometric to tell you that you may be ill before you even know it. But for some, these four superpowers could be more easily recognised as the four horsemen of the apocalypse, bringing disruption, danger and an end to the world as we know it.

In the UK this week, the Trade Union Congress (TUC) is calling for a four-day week, leveraging the efficiency opportunities that technology brings to allow people to work four days instead of five and, importantly, be paid the same amount for producing the same output in a shorter time through the application of technology. Some would argue that the ability to produce more at the same cost with the same resources is the very definition of growth, but the suggestion of the shorter working week gives away the underlying concern that eventually, on some level, most jobs that are done by unionised staff will be replaced by technology. Driverless trucks and taxis are already in use and will likely change the way goods and people are transported forever. The next generation will no doubt marvel at the novel idea of driving their own car in the same way children today look at phones that connect to a wall socket.

Looking at a specific industry, real estate agency markets have come under significant pressure from market disruptive technology

providers. Anyone wishing to sell or let their house can employ an online agent and manage most of the process from their mobile device, transferring the largest asset people would normally own, without the assurance of the lawyer and agent effectively indemnifying them against a poor deal. Much of the success of this is down to the application of technology users are already comfortable with, allowing them to move what they had previously considered as a risky and complicated transaction into their own control, using widely adopted technology and mediums.

Expand that idea into the securities finance market and consider how data and technology are allowing growth in efficiency, but also, to an extent, threatening the status quo. In a recent meeting with a client, the securities lending manager introduced herself as the European head of securities finance and collateral management and equity execution—a title that reflects not only her substantial capabilities but also the integration of the securities finance business unit into a more integral component of the bank itself. Enterprise collateral management, a term not heard of a few short years ago, has ensured that the securities finance desk of a bank is often now directly responsible for the provision of collateral across a number of other business disciplines.

With the best will in the world, securities lending, as was, could not really be described as a dynamic industry, taking years to adapt to structural changes rather than months. However, as it becomes increasingly integral to the wider workings and disciplines of the parent bank or financial organisation, it is having to adapt their timescales and meet their expectations. Technology will begin to merge and providers like FIS are adapting to meet that need, delivering concept systems that allow multiple trading activities from one browser. While much of this change may be being pushed on the industry by regulatory changes, there are other pressures happening outside the banks that, if ignored, will disrupt the market just as online estate agents have put power into the client's hands.

New exchange-like services, offering all-to-all or peer-to-peer financing solutions, are growing in their influence. Central counterparty (CCP) clearing houses, which as a concept have been around for longer than many care to admit when explaining bilateral trading to non-securities financing types, still carry only a small proportion of the market flow, but will most likely turn those proportions on their heads in just a few years. There is a multitude of reasons why this will happen, but to note is the increasing engagement of beneficial owners and the impending arrival of the single counterparty credit limit (SCCL) expected in January 2020.

Beneficial owners, at least the leaders of that group, see securities lending revenues as an integral part of their investment product, and with increased engagement comes a glut of supply, particularly of cheap liquid general collateral assets. To keep revenues meaningful, beneficial owners will be seeking cheaper and more direct routes to market. Note the recent announcement of zero-fee funds from Fidelity Asset Management; they will almost certainly be looking to securities lending revenues to offset the loss of fees and given the announcements impact on their share price and that of their competitors, they have started a race to the bottom on fees that will force greater numbers of assets into lending.

The SCCL will apply a 15 percent exposure limit for Globally Systemically Important Banks, based on tier-one capital, on any individual counterparty, which means that more profitable lines of business will get the first claim on such limits, particularly when it is noted that the SCCL does not apply to CCPs.

It is far from news to state that the industry is currently more than fixated on the impending arrival of SFTR, and other jurisdictions' application of the Financial Stability Board's transparency directive. However, the industry must not ignore the other activities going on outside its gates and instead leverage the efficiencies that the four superpowers of technology can bring to our market, for the benefit of our clients and our business, even if it means we will still have to work five days a week. **SLT**

"The industry must not ignore the other activities going on outside its gates and instead leverage the efficiencies that the four superpowers of technology can bring to our market"

David Lewis
Senior director
FIS

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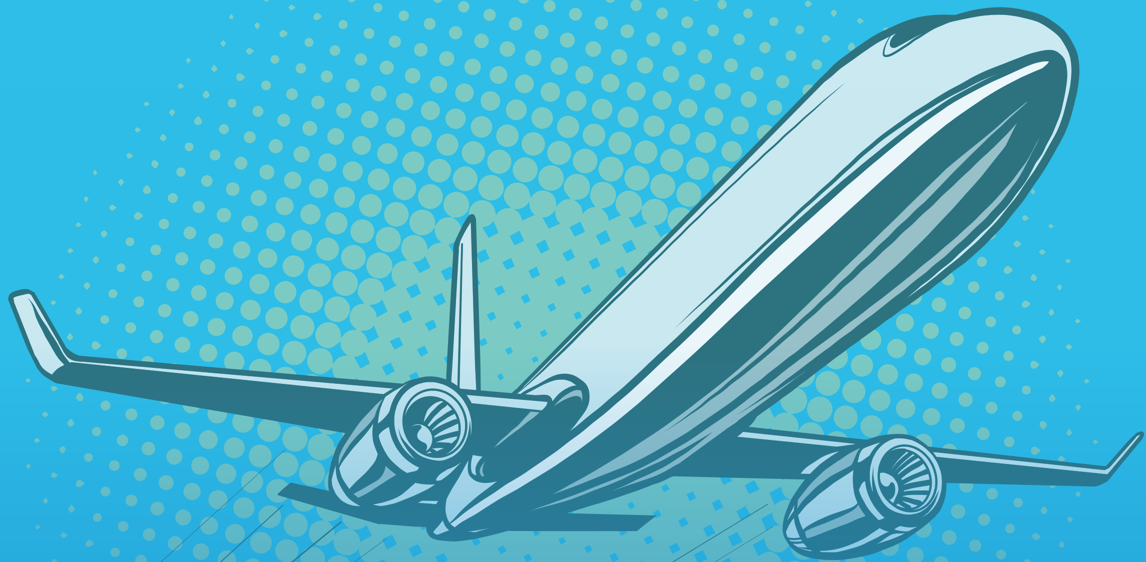

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Comings and goings at SIX, State Street, Lago Kapital and more

The International Securities Lending Association (ISLA) has appointed Richard Colvill to work exclusively on the Securities Financing Transactions Regulation (SFTR).

Colvill has significant experience in delivering complex data projects within securities finance over a 20-year career and will be working alongside Sarah Nicholson to help the industry develop standardisation and consensus around the SFTR reporting on behalf of ISLA.

According to ISLA, this significant additional commitment will allow ISLA to take a leading role in developing market wide consensus around several aspects of SFTR including unique transaction identifier creation, data fields, lifecycle events, data transfer timelines, messaging protocols and collateral processing.

Andy Dyson, CEO of ISLA, commented: "I am delighted that Richard Colvill is joining us at a pivotal moment in the history of the industry. Non-compliance with this mandatory reporting obligation is not an option and Colvill's arrival will significantly enhance our capabilities over the coming months."

Commenting on his new role, Colvill said: "This is a great time to be joining ISLA. The association enjoys an excellent reputation and it has become increasingly obvious over the last few months that the industry is looking to them for direction, to navigate through the complexities of this [SFTR] legislation."

He added: "I feel privileged to have the opportunity to join this dynamic team and to help provide leadership with this exciting incentive, and look forward to the challenges."

Lago Kapital has hired Jesse Karjalainen as senior data scientist to support Lago Kapital's data science department.

Based in Helsinki, the location of Lago Kapital's headquarters, Karjalainen will report to Jarkko Järvitalo, founder and CEO. Lago Kapital is an independent securities finance broker based in Finland and regulated by the Finnish Financial Supervisory Authority, specialising in Scandinavian and Eastern European markets.

Nikola Todorovic has left SIX Securities after eight years as head of sales and relationship management, securities finance.

It is understood Todorovic has moved to another bank in Zurich and has been appointed to a broader securities service role that covers securities finance, cash and custody.

Todorovic has previously served at Aramid Capital Partners and ABN Amro Mellon.

Johnnie Peacock has been appointed as post-trade sales and strategic account at FIS, effective September.

Previously, Peacock served as regional manager and strategic accounts at Lombard Risk. He served in the role from February 2017 to July 2018.

He has also served as client services director at Broadridge, clients manager at State Street and a consultant for securities finance at UBP.

Hazeltree, a provider of integrated buy-side treasury management solutions, has appointed Askin Leung as managing director and head of Hazeltree Asia Pacific (APAC).

Leung will be based in the firm's Hong Kong office and will lead Hazeltree's expansion in the APAC region, as Hazeltree plans to expand this office and increase staffing over the next year.

Leung has a background in buy-side financial technology solutions as both a supplier and client and has been at Broadridge/Paladyne for the last ten years.

He launched the investment management solutions business at Paladyne Systems in the region and oversaw its growth as a market leader until it was acquired by Broadridge Financial Solutions in 2011.

In 2016, Leung's role was expanded to include Broadridge's sell-side North Asia business as general manager in Hong Kong.

Earlier in his career, he served as the head of implementation for APAC at Linedata Services/Beauchamp, a provider of portfolio management software.

Sameer Shalaby, president and CEO, commented: "We are excited about adding Askin Leung to our management team. He brings a wealth of insights and on-the-ground experience in the APAC markets."

He added: "Leung will play an important role in responding to the increased demand for Hazeltree's treasury solutions in the region, to help our clients improve operational efficiencies, reduce counterparty risks and incrementally generate alpha from their treasury and portfolio finance functions."

Commenting on his new role, Leung said: "My goal is to focus on existing customer needs first, while we expand our sales activities across the region."

"We are seeing an increased demand for Hazeltree's innovative treasury solutions and I am excited to be joining the firm at this important juncture."

He added: "I see a significant opportunity to help our customers reduce their operating costs and improve counterparty exposure management while capitalising on treasury and portfolio finance alpha opportunities." **SLT**