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Eurex to expand repo partnership programme

Eurex Clearing will expand its partnership programme to cover the repo and over-the-counter (OTC) foreign exchange segments.

Eurex announced its plans following the initiation of Eurex's OTC interest rate derivatives segment, which started in January 2018.

As part of its partnership programme, Eurex Clearing shares governance and economics with the most active programme participants.

For the repo segment, the aim of the programme is to increase choice and efficiency for market participants in special repo and general collateral instruments and to foster adoption and growth in the dealer-to-client repo business.

The new FX segment of the partnership programme is designed to deliver the benefits

of clearing to OTC FX markets, which are still largely uncleared today.

Eurex Clearing is currently working with market participants to be the first major clearing house to offer a comprehensive cross currency swap clearing service.

Market participants can now register their interest to join the new programme components for a planned start in Q1 2019.

Commerzbank, Deutsche Bank, J.P. Morgan and Morgan Stanley have expressed an early interest to join both new segments—repo and OTC FX.

In addition, Citigroup, DekaBank and Landesbank Baden-Württemberg have indicated their interest in participating in the repo programme.

Erik Müller, CEO of Eurex Clearing, commented: "The extension of the partnership programme further enhances choice and innovation in the marketplace."

He added: "Market participants now can tap the full benefits of Eurex Clearing's integrated value proposition across fixed income derivatives, repo and FX markets."

Charles Bristow, co-head of global rates trading at J.P. Morgan, said: "J.P. Morgan has been an early supporter and design partner for the OTC interest rate derivatives clearing segment of the partnership programme."

He added: "We welcome the planned extension of this successful programme which is aimed at broadening market participants' clearing options for the new asset classes and increasing resiliency."

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Company Profile

Matthew Chessum of Aberdeen Standard Investments runs through the businesses success since its merger in 2017

page 17



Conference Report

At the Annual Collateral Management Conference, panellists discussed how to prepare for the future of collateral management

page 19



Country Profile

Russia has seen increases in the value of repo transactions, FOP transactions, and positive hedge fund returns.

page 21



Insurance Solutions

Alan Ball explains how insurance can be used to bridge the gap between agent lenders and their clients

page 25



Technology Update

Matthew Battaini of Helix discusses the company's efforts in the industry and the future of technology

page 27



Data Analysis

Sam Pierson of IHS Markit discusses how CYBG's acquisition agreement with Virgin Money created an excellent opportunity for shareholders

page 29



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Kaizen Reporting launches regulatory reporting training

Kaizen Reporting is to launch a training service focusing on regulatory reporting requirements under the Markets in Financial Instruments Regulation, the European Market Infrastructure Regulation (EMIR) and the upcoming Securities Financing Transaction Regulation.

The training service will be led by Kaizen's recently appointed senior regulatory reporting specialist, David Nowell.

Nowell previously served as a transaction reporting technical specialist at the UK Financial Services Authority, as head of transaction reporting for a tier-1 investment firm, and head of compliance for an approved reporting mechanism and trade repository.

Nowell also has experience in client training for MiFIR transaction reporting and EMIR trade.

SSE promotes guidelines for services of bond collateral disposal platform

The Shanghai Stock Exchange (SSE) has issued and implemented guidelines for the services of a bond collateral disposal platform in order to improve the mechanism for bond collateral disposal.

SSE said the guidelines will protect the legitimate rights and interests of investors, and promote the healthy development of the exchange-traded bond market.

In recent years, the exchange-traded bond repo market has developed rapidly and a multi-level repo business system has formed, noted the SSE.

SSE said: "The size of collateral in the repo transaction category has grown significantly, the number of market participants has expanded and the overall operation of the repo businesses has been stable, safe and controllable."

It added: "The centralised platform will provide collateral disposal services for the market and further improve the institutional mechanism for the exchange-traded repo market."

"The platform is of great significance to the long-term healthy development of the bond market."

The SSE said the guidelines stipulate the business norms of the platform in the scope of application, the underlying assets of the disposal, the participating entities,



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the application and announcement for the disposal service, disposal arrangements and other aspects.

SSE also stated the introduction of implemented guidelines will effectively improve the liquidity of collateral, meet the need of market institutions to quickly dispose of collateral, and protect the legitimate rights and interests of investors.

Items for disposal include collateral products such as treasury bonds, local government bonds, financial bonds, corporate bonds, enterprise bonds, convertible bonds, asset-backed securities and other SSE-approved bonds.

The SSE concluded by saying that in the near future, it will make efforts in training and promotion for the platform.

It said that it will continue to make improvements, optimise the mechanics of bond collateral disposal, increase disposal efficiency, fully protect the legitimate rights and interests of all the parties in repo.

BBH: the impact of US-China trade wars on securities lending

The US tariffs target high-end technology products made in China, which could have a long-term impact on securities lending, according to a recent blog published by Brown Brothers Harriman (BBH).

The blog, which reviews the potential impacts of the US-China trade wars on securities

lending, said US tariffs could mean that companies such as Apple and Lenovo that operate significant Chinese production bases, face higher costs or supply-chain disruption.

Tesla is one company at risk, BBH stated, as it relies on American-made vehicles for all its Chinese sales.

BBH said other US car makers such as General Motors and Ford also manufacture in China.

Securities lending demand has been strong for issuers of Chinese American depository receipts/shares such as Cango, Aurora Mobile and Pinduoduo.

The biggest European impact from a securities lending perspective is from the mining and exploration companies, said BBH.

The 10 percent tariff on steel and 25 percent tariff on aluminum has had a substantial effect on the percentage of free float on loan.

BBH affirmed: "We have also seen demand driven from threats of Trump imposing tariffs on European cars. Germany is clearly most concerned with a possible 20 percent tariff to be imposed which has given a strong rise in percentage of free float on loan in Volkswagen and BMW."

BBH went on to discuss that the current securities lending demand in Asia has been focused in Hong Kong, Japan and Taiwan.

It said: "We have seen over a 50 percent increase to the percentage of free float on

loan in a wide range of Chinese and Japanese manufacturing companies such as AAC Technologies, Weichai Power, Fuyao Glass, Shenzhou International, Mitsubishi Chemical, Honda Motor Co and food and beverage company, Suntory."

"Like the US market, all these stocks are very liquid in the Asian securities lending market so have remained trading at low fees. We have seen that most stocks with an increase in percentage of free float have remained at low fees due to high liquidity in the lending pool."

BBH concluded: "In the short run, as the equity markets seems to have shrugged off the tariffs, there is likely to be limited impact for securities lending."

"In the longer term, as the tariffs start to affect company financials, essentially through higher cost of production, we would expect short demand to return and with greater conviction."

CGS expands CUSIP Options

CUSIPS Global Services (CGS) has expanded its options service to include futures and options on futures for the North American market.

Exchange coverage for this new data set includes Chicago Board of Trade, CBOE Futures Exchange, Chicago Mercantile Exchange Inc, New York Mercantile Exchange—Comex Division, Eris Exchange, Bourse de Montreal Inc, Minneapolis Grain Exchange, Nodal Exchange, Nasdaq Futures Inc, ICE Futures US and New York Mercantile Exchange.

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CGS said that by assigning CUSIP identification to futures and options on futures, it will enable market participants to streamline their pre- and post-trade reporting requirements under the second Markets in Financial Instruments Directive and European Market Infrastructure Regulation mandates.

It said the use of CUSIP identifiers in this market will also simplify back-office operational processes by introducing the universally recognised and accessible nine-digit CUSIP taxonomy.

Matthew Bastian, director, market and business development and west coast operations at CUSIP Global Services, commented: "The addition of futures and options on standard futures into the CUSIP Options Service is an important step forward for transparency and accessibility in the futures markets."

He added: "Not only will this new coverage help global firms track futures and options on futures more efficiently, it will help to standardise the identification processes currently being used in these markets."

Preqin: global assets will grow by 2023

By 2023, private equity will be significantly larger than today, according to specialist data firm, Preqin.

In a new paper published this week covering the future of alternatives, Preqin predicted that by 2023, global assets under management will stand at around US \$14 trillion.

Mark O'Hare, chief executive of Preqin, predicted there will be 34,000 fund management firms active globally (a rise of 21 percent versus 2018).

Preqin said the growth will be dependant on alternatives' track record and ability to deliver superior risk-adjusted returns to investors as well as investors' need for alpha—whether that is found in private capital or public markets.

Preqin predicted growth will also be dependent on the steady decline in the number of listed stocks, as private capital is increasingly able to fund businesses through more of their lifecycle, Preqin said.

The data firm stated that the importance of technology in the future should also not be underestimated.

It said: "Technology (especially blockchain) will facilitate private networks and help investors and fund managers transact and monitor their portfolios, and reduce costs versus public markets."

Preqin added: "The mass affluent around the world would like to increase their investment in private capital if only the structures and vehicles (and regulation) permitted; technology will help."

Northern Trust securities lending revenue slips in Q3

Northern Trust's securities lending revenue dropped to \$24.1 million in Q3 2018 from

\$30.2 million in Q2 2018, according to the company's Q3 results.

This reflects lower spreads and volumes in the current quarter, primarily due to the international dividend season that occurred in the previous quarter.

Net income was \$374.5 million, compared to \$298.4 million in Q3 2017 and \$390.4 million in Q2 2018.

Assets under custody and/or administration inched ahead to \$10.15 trillion from \$10.06 trillion in the previous quarter.

Custody and administration fees slipped to \$108.7 million from \$30.2 million in the previous quarter.

Northern Trust said that this was primarily due to the unfavourable impact of movements in foreign exchange rates and lower transaction volumes, partially offset by favourable markets.

Michael O'Grady, president and CEO, said: "Northern Trust's third quarter 2018 performance produced earnings per share growth of 32 percent compared to last year and a return on average common equity of 15.1 percent."

He added: "Trust, investment and other servicing fees, net interest income, and foreign exchange trading income all delivered strong year-over-year growth while the company also produced positive fee and total operating leverage versus last year."



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BNY Mellon reports mixed Q3 results

BNY Mellon has reported a total revenue increase of 1 percent to \$4.1 billion in Q3 2018, compared to \$4.0 billion in Q3 2017.

On top of the revenue increase, BNY Mellon's results also show that fee revenue increased 1 percent and net interest revenue increased 6 percent.

Total non-interest expense increased by 3 percent to \$2.7 billion.

Continued investments in technology were partially offset by decreases in other expenses, while litigation expenses increased by 2 percent per common share.

Assets under custody and/or administration rose by 7 percent to \$34.5 trillion. Assets under management increased slightly to \$1.8 trillion.

Charles Scharf, chairman and CEO, said: "While we continued to benefit from a reduction in our tax rate related to the new tax law in the US and from strong capital returns, our revenue growth was modest."

"We did see reasonable growth in some of our businesses and remain confident that we can increase the rate of growth in the others."

He added: "We are moving with a sense of urgency to improve our growth trajectory. Bringing in new talent to complement the great expertise we already have is critical."

"Knowing it will take time to increase our organic revenue growth, we remain keenly focused on expenses and continue to believe there are meaningful opportunities to become more efficient in both the short and the long term, which will help fund investments to improve the quality of our work and build additional capabilities for our clients", Scharf concluded.

Views needed on leverage ratio treatment of client cleared derivatives

The Basel Committee on Banking Supervision (BCBS) has called for stakeholder views on the leverage ratio treatment of client cleared derivatives under Basel III.

The call comes alongside a consultative document, which considers opportunities to prevent excessive leverage, improve the quality and quantity of capital in the banking system, and promote central clearing of standardised derivatives contracts.

The leverage ratio complements the risk-based capital requirements by providing a safeguard against unsustainable levels of leverage, mitigating gaming and model risk across both internal models, and standardised risk measurement approaches.

As part of the finalised Basel III reforms published in December 2017, the committee noted that it would conduct a review of the leverage ratio's impact on banks' provision of derivatives client clearing services and any consequent impact on the resilience of central counterparty clearing.

BCBS has opened its review seeking the opinion of stakeholders on whether a revision of the leverage ratio's treatment of client cleared derivatives may be warranted.

Stakeholders are invited to provide "concrete and robust empirical evidence" to support their views.

The committee said it may consider a range of treatments, including no change to the current treatment and an amendment to the treatment of client cleared derivatives to allow cash and non-cash initial margin received from a client to offset the potential future exposure of client cleared derivatives.

The committee might also consider the alignment of the treatment of client cleared derivatives with the standardised approach for measuring counterparty credit risk exposures.

BCBS said this would have the effect of allowing both cash and non-cash forms of initial margin and variation margin received from a client to offset the replacement cost and potential future exposure amounts of client cleared derivatives.

European repo market grows

The European repo market continues to grow, with the baseline market size at a record €7.4 billion, according to a survey by the European Repo and Collateral Council (ERCC) of the International Capital Market Association (ICMA).

The survey, which calculates the amount of repo business outstanding on 6 June 2018, from



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the returns of 62 offices of 59 financial groups, showed an increase from €7.3 billion in December last year to €7.4 billion in June this year.

These figures represent an increase of 13.9 percent since last year's survey in June.

Godfried De Vidts, chair of ICMA's ERCC, commented: "The repo market continues to perform as a collateral source for prudential and regulatory requirements. Highly liquid, unencumbered flows of collateral already help to protect the central counterparty and bilateral hedging flows that are so crucial for the real economy."

He added: "Further mandatory clearing obligations for the buy-side will also need the repo market to deliver collateral. All-in-all, growth in repo activity is positive for global financial markets."

The growth in repo business over the last two surveys is said to be down to the increased

requirement for collateral to underpin financial transactions beginning to bite.

Post-crisis regulation mandated by the G20, according to ICMA, has pushed markets towards centralised clearing, with the associated higher margin commitments and more frequent margin calls creating huge collateral demands.

The sell-side has already adopted this mandatory obligation while the buy-side is being brought on board, with the final deadline in 2020.

The survey found that the increase in repo market size noted by the December 2017 survey and sustained in the first half of 2018, indicates that the market has adapted to a series of new regulations implemented in recent years and the business is growing, with more efficient collateral management delivering improved profitability for repo traders.

However, it showed evidence of this being a market under stress and it remains to be seen if further proposed regulations can be assimilated successfully.

It also found that the overall recovery in electronic trading suggests a recovery in interdealer business. However, triparty repo has not shared that recovery and its share of the survey sample fell back to 6 percent from 8.6 percent in December last year.

According to ICMA, this reflects the continued dampening effect of plentiful central bank liquidity on the need for market funding.

ESMA publishes their first EU derivatives report

Trade repositories reported a total of 74 million open transactions at the end of 2017, amounting to a gross notional outstanding of around €660 trillion, according to European Securities and

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Markets Authority (ESMA)'s first annual statistic report on the EU's derivatives markets.

These statistics included both over-the-counter (OTC) and exchange traded derivatives.

The report, based on data submitted under the European Markets and Infrastructure Regulation (EMIR), provides the first comprehensive market-level view of the EU's derivatives markets.

It includes sections on market monitoring providing an analysis of structures and trends in the European derivatives markets, building on the indicators developed for risk monitoring; statistical methods dedicated to topical issues in developing and exploring derivatives data and derivatives market statistics.

In notional terms, interest rate derivatives dominated the market, with 69 percent of the total amount outstanding, followed by

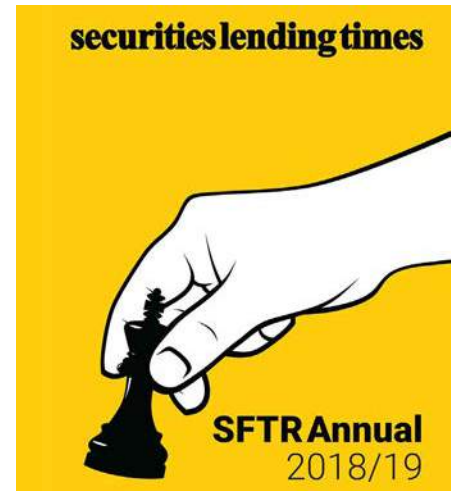
currency derivatives, at 12 percent, while all other asset classes, that is equity, credit and commodity derivatives, account for less than 5 percent of the total amount outstanding.

Central clearing rates for new transactions have been increasing significantly, demonstrating the effectiveness of the EMIR clearing obligation.

For all outstanding contracts in Q4 17, central clearing rates were around 27 percent (25 percent in the first quarter of 2017) for credit derivatives and 58 percent (40 percent in the first quarter of 2017) for interest rate derivatives, including contracts concluded before the clearing obligation came into force.

Steven Maijoor, chairman of ESMA, said: "The data gathered by ESMA as part of its EMIR responsibilities provides us with an unprecedented level of detail on derivatives transactions and exposures."

He added: "ESMA's analysis of this data provides, for the first time, new information about this market, which will facilitate oversight and enhance supervisory convergence, thereby contributing to orderly markets and financial stability in the EU."



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Keep calm and carry on

Matthew Chessum of Aberdeen Standard Investments runs through the businesses success since its merger in 2017 and provides an overview of the current market, where regulation and Brexit are hot topics

Justin Lawson reports

How has the business changed since the merger in 2017?

The merger between Aberdeen Asset Management and Standard Life Investments lead to the creation of the largest independent asset manager in Europe. Currently, the combined entity administers £610 billion of assets worldwide across a number of different asset classes. Aberdeen Standard Investments remains a high conviction, long-term investor seeking to realise the value of investments over time. This strategy filters all the way down to our securities lending programme. As an investor, we tend to hold fewer positions but in larger sizes compared to our competitors. As a result, we tend to try and lend only where it makes sense from a returns perspective favouring fewer stocks on loan but at above average fees.

The merger has given many teams the opportunity to cherry-pick the best practices from each heritage as well as increasing both the amount of assets under management and our range of asset classes that are invested in. This is therefore a great opportunity to improve upon past processes and ensure that we are well positioned for future challenges. We are expecting the lending book to grow as the heritage Standard Life fund ranges are not currently in any lending programme.

We are in the process of agreeing a new company-wide approval process for securities lending to ensure that as many funds as possible are given the opportunity to join our existing programme. Securities lending has now moved internally from the dealing desk into the liquidity management team sitting alongside the money market and collateral management functions. Putting these together will allow us to use securities lending and repo more efficiently to manage our collateral positions and to become more complex in the collateral management and securities lending solutions that we are able to offer to the other teams internally within Aberdeen Standard Investments.

How does your securities lending programme work?

We lend through multiple lending agents and divide our programme by fund ranges. We run both discretionary and exclusive programmes as we like to lock in guaranteed revenues on lots where we are being offered additional outperformance in relation to market benchmarking. We don't do anything in-house but that's not to say that we never would.

The development of our collateral management competences may give rise to additional infrastructure that we did not previously have. This may give us the option of becoming a direct lender into the market for certain asset classes in the future.

At the current time, however, we still see a great deal of value in the services offered by our agent lenders especially when you start to think about the amount of heavy lifting they do on fairly slim margins. The indemnity that they provide also gives our fund boards an extra level of protection and comfort.

What is the main purpose of your securities lending programme and how risk-averse is it?

Securities lending adds additional incremental revenues to our funds and consequently the clients and customers invested in the funds. It adds a handful of important basis points to a fund's performance in a risk adjusted manner. Securities lending isn't a driver of investment decisions and is certainly not part of any complex strategy to add additional risk and/or high levels of return through convoluted reinvestment or synthetic structures.

All beneficial owners will tell you that their programme is risk-averse but given our lending style, our agent indemnification provisions, our BBB+ minimum counterparty rating, our collateral margins and finally our collateral profile, we do certainly look to minimise as much risk as possible. We are also actively involved in the oversight process and conduct regular review meetings with our agents to go through any issues. We run quarterly stress testing of our on loans versus collateral positions and work closely with our agents to ensure that they remain focused from both a risk and revenue perspective.

As the largest asset manager in the UK, what advantages does this bring?

Big is definitely better in the asset management world at the moment. The drive for greater economies of scale is leading to a number of mergers between previous rivals. Being part of a larger entity brings wide ranging advantages to an organisation. Understanding and working through the impact of regulation is one benefit of having access to greater resources as well as investment in new technologies. Specifically to the lending programme, however, the diverse range of assets that we now have in our programme

and its overall size help us to attract better fee splits, access to indemnification at a cheaper price, and a seat around the table when new initiatives are being rolled out.

We also have better and more diverse expertise to aid in the oversight process. Finally, being a large organisation means that we have many teams interacting in many different areas of the financial markets. This interaction provides us with a broader access to financial and market information in general which helps us to keep agent lenders and borrowers honest in their dealings with us.

How has the European market been performing for you with all the Brexit concerns?

Europe is still showing value from a securities lending perspective. UK infrastructure borrows seem to be producing most of our revenues in this region. We recently started lending in Russia, which has been very profitable as demand is robust and fees are above average. Turkey is showing some value given the recent economic difficulties but within Europe we tend to concentrate on the scrip opportunities and those stocks that have the higher lending rates attached to them.

In terms of Brexit, so far we haven't seen too much impact. Our agent lenders may face some degree of repapering with some borrowers and depending upon how the negotiations conclude there may be some stocks that may come under a degree of "Brexit pressure" but at the moment we haven't seen anything to note.

Is Asia still an important market for you and how has that region been performing?

A lot of revenues for the funds over the last few years have come from Asian stocks. Singapore, Hong Kong, Japan and Thailand have all provided some strong revenue opportunities. Our stronger earning funds include our Asian small cap portfolio and our Chinese equity fund. Asia provides a good percentage of our overall revenues and holds a lot of potential for us. We would like to be active in Taiwan and Malaysia but the pre-sale notifications prove difficult for us to manage.

I understand that the Philippines stock exchange is looking into a securities lending solution for offshore investors and we would definitely be a keen participant in this if it does ever come to fruition.

What concerns do you have with current regulations?

In terms of regulation, I don't see anything too prohibitive on the horizon. The Securities Financing Transaction Regulation (SFTR) is being covered mainly through our lending agents although we do have our own internal capabilities. The guidelines for this are already in place and were just waiting for the final trigger to be pulled. There has been a lot of talk about the Central Securities Depositories Regulation (CSDR) and the introduction of mandatory buy ins in Europe. Many participants seem to be quite concerned about this but I believe that the incoming SFTR reporting requirements will help to increase settlement rates anyway. When looking at CSDR it is also important to remember that we already successfully operate in a number of jurisdictions around the world where similar market practises already exist.

Any predictions for the market in 2019?

2019 will be an interesting year from a securities lending perspective. As pressures on asset managers fees continue there will be further consolidation in the asset management world. I therefore expect the increase in the amount of assets that are available in lending pools to keep increasing. I can see 2019 offering better market conditions for stock to trade more "special". The rising interest rate environment is likely to take its toll on some corporations that have thrived on cheap debt in the past few years so some companies shares may start coming under more pressure. Brexit, depending upon the deal that the UK government negotiates, if at all it does manage to, will also have an impact upon the UK market. Much like the morning after the referendum result, if Britain slides out the EU without a deal, the FTSE 250 and AIM stocks are bound to see a lot of downward pressure. Once again it will be time for that old British adage to come into play: keep calm and carry on. [SLT](#)



I can see 2019 offering better market conditions for stock to trade more 'special'



Matthew Chessum

Investment manager, securities lending, collateral management, money markets
Aberdeen Standard Investments





All change, please, all change

As delegates hit Amsterdam for the 12th Annual Collateral Management Conference, panellists discussed how to prepare for the future of collateral management and what could be learned from the past

Jenna Lomax reports

Deliberations around initial margin trends and the popularity of outsourcing collateral processes were high on the agenda for this year's 12th Annual Collateral Management Conference, as was Brexit and debate on the use of machine learning within collateral management.

On the first morning of the conference held in Amsterdam, a representative from LCH, discussed clearing's reputation both within and beyond securities finance.

He said: "Most people think clearing is mandated and is not the greatest thing on Earth, but people have come to realise the benefits of clearing, especially given that today, globally, 70 to 80 percent of the world's derivatives are now cleared."

"People have come to realise the benefit, more now than compared to 25 years ago, and there are economic drivers around this", he said, naming Brexit as the main economic driver currently.

The speaker clarified three initiatives that LCH is trying to implement in the run-up to the Brexit deadline and beyond.

Firstly, he said: "LCH is applying for authorisation as a third country central counterparty (CCP) under the European Market Infrastructure Regulation", but he said the challenge there is, "as

long as the UK is not a third country, we can't really apply—the timeline is a challenge".

The second point, he said, was a consideration of that timeline. He stated: "We want to make sure European members and clients benefit from, and have access to, global pools at LCH—to clear where they want to clear."

"[LCH] is optimistic—regulators are recognising our challenge. The Bank of England has already granted temporary recognition to European CCPs for three years after Brexit."

Thirdly, he remarked that not allowing Euro clients access to LCH or other UK CCPs, will lead to fragmentation of markets, which he warned, could result in "higher cost and risk to financial stability".

In a separate panel, panellists discussed the impact Brexit could have on the collateral market.

One moderator asked: "As the March deadline of next year looms, Brexit still lies among a lot of negotiation, we don't know what Brexit is going to look like, it could have any kind of impact on the market, but what about the collateral market?"

One panellist explained, from a counterparty perspective, that if a counterparty is located in the UK, you need to "repaper your

documents towards a European entity to be able to move from one jurisdiction to another”.

But he added: “There is significant risk related to that especially if it is located in the UK, it could be quite a hostile environment after Brexit.”

An audience member also stated that this description of a hostile environment was also a concern when considering CCPs.

He said: “I work for a vendor, but Brexit could mean certain businesses having to initiate a CCP in mainland Europe and possibly a CCP in the UK, also”, which he indicated “means two quotes from brokers—meaning more complexity and more cost”.

But the panellist also said that the “impact could be overestimated at the moment. It could remain just political”.

“We’ll know by March, but firms should prepare for any outcome”.

Responding to a question on collateral outsourcing, more than half of the 50 delegates asked stated that they had not yet outsourced any part of their collateral process within their firm.

To this result, one panellist stated: “It would be interesting to see what percentage of those people who said ‘no’ are still doing business completely manually.”

Another panel, still on the topic of collateral, heard delegates discuss the investigation of disputes on collateral calls.

“We’re not exactly hiding away, but we aren’t doing enough to investigate disputes on collateral calls”, said one panellist, when asked what were his day to day challenges of collateral management.

The panellist, head of collateral management at a Nordic-based asset management firm, said that more collaboration was needed in these disputes.

He said that one particular problem was that collateral portfolios are not being aligned well enough.

The moderator also asked the panel how they calculated initial margin calls, to which the head of collateral said he used an external firm to enhance delivery, though he affirmed he did not receive calculations from all of them, as not all calculations were done in-house at his firm. However, he said: “We fully trust our outsource company to do so.”

When the conversation moved on to the consideration of certain security portfolios, one panellist said he used government bonds to a large extent, but indicated there is a question of how liquid these can be and indicated regulation is trying to enhance this. He stated that regardless of your firm’s level of compliance, “you should always have to ensure you are aware of who knows what—there needs to be clarity on ownership”.

The panel then gave their views on how important it was for their firm to keep vendor margin calculations in-house, and if they would consider using a third party.

One panellist said: “From a buy-side perspective, there’s no reason for keeping calculations in-house.”

“If we get rid of portfolio disputes, and have complete collateral efficiency, you shouldn’t have to look at your collateral on a daily basis.”

He added: “Looking further into the future, it could be developed as a cloud-type system—having one central cloud system could be extremely beneficial. If I have to provide extra information I will, it’s easy to talk to counterparties about it.”

Another panellist agreed that a central utility would greatly help, but he said he wouldn’t hold his breath waiting for that to happen, because “in some places, the industry still uses faxes” for collateral purposes.

In a panel looking to the future of collateral management, a speaker from a Swedish bank discussed collateral’s future potential impact on the stability of the global economy.

With a visual of the Mel Gibson film, *Maverick*, he indicated how collateral has been used in poker games for decades, even as far back as the Wild West.

He described that in the game of poker, collateral has also been needed as an insurance.

He stated it is an “important defaulter and should pay its mistake from the 2008 financial crisis”.

Historically, he said, whether by loan or contract, collateral was initially traded in physical forms, this moved in to ledgers, which was then followed by the introduction of the stock exchange in the 1920’s, before the Great Depression in 1929.

He continued: “Before the Financial Crisis of 2008, the collateral process was mainly in line with the market from spreadsheets to email.”

He went on to explain the current challenge of fragmentation and the collaboration he had seen for integration across the whole industry, to make the process fully automated.

He concluded: “Talking about the future is both an easy and difficult topic, you can’t be right or wrong.”

“But it is also difficult because you have to predict and plan for something you don’t know.”

Though he stated regulators should be able to move forward, making smart regulations, to meet responsible targets to counter risk to reach “that golden state” [SLT](#).



REFLECTING ON RUSSIA

Russia's securities finance industry has enjoyed growth recently, with increases in the value of repo transactions, FOP transactions, and positive hedge fund returns. Now the country aims to lay down the foundations for the development of the digital economy

Maddie Saghir reports

As 2018 begins to draw to a close, it is worth reflecting on Russia's securities lending landscape over the last 12-24 months. The largest country in the world achieved much in 2017 and it is continuing to grow and develop, with aims to lay down a foundation for the development of the digital economy and to ensure the emergence of new asset classes for investors.

At the beginning of the year, Russia's National Settlement Depository (NSD) revealed its 2017 annual results, which found a 12 percent increase in the value of repo transactions compared to the previous year. In April, Russia's Federal Treasury successfully conducted its first repo auction with a floating rate via NSD's collateral management system. Then later that month, Russia's central securities depository received the status of authorised depository of Belarus. The authorisation allowed NSD to record the rights to government securities issued by the Ministry of Finance, on behalf of the Republic of Belarus. Most recently in October, it was reported that, internationally, Russia-focused hedge funds surprised in September with positive returns of 3.75 percent.

Russia's NSD explained that their clients are showing a greater interest in foreign securities. In 2017, the number of foreign securities issued in custody at NSD increased from 5,100 to 8,500. The number of free of payment (FOP) transactions at the international central securities depository (ICSD) grew by 10 percent, while the number of delivery versus payment (DVP) transactions at ICSDs surged to 74 percent.

In late 2017, as part of efforts to improve foreign securities services, NSD launched a new service for individual accounts with ICSDs, to allow for segregated holding of clients' securities through separate accounts held by NSD with Euroclear Bank.

A spokesperson for the NSD said: "The key advantages offered by the new service include the possibility to segregate assets in a separate account, availability of additional services that can be used at ICSDs (such as technical netting, transaction linking, and instruction prioritisation), which contributes to a higher liquidity and makes it possible to fund the trade right before the settlement, rather than in advance."

On the theme of reflection, the NSD explained how collateral management services have developed over the last 12 months. The spokesperson said: "In 2017, there was a reshuffle in the market of liquidity providers using the collateral management system (CMS) services".

"On the one hand, the Bank of Russia switched from supplying to absorbing the liquidity. The discontinuance of liquidity auctions and the dear-money policy pursued by the Bank of Russia resulted in a sharp drop in the volume of Bank of Russia's repo trades with collateral management: from RUB 9 trillion (\$136 billion) in 2016 to RUB 688 billion (\$10 billion) in 2017."

"On the other hand, the Russian Federal Treasury continued its increasingly active involvement in financial market transactions. For the purposes of Federal Treasury repo trades, NSD made a number

of improvements resulting in a wider range of securities that could be accepted as collateral."

Meanwhile, in April 2017, NSD offered CMS Web-client, an integrated solution for over-the-counter (OTC) repo trades, incorporating state-of-the-art software for clients, to new types of market players: brokers, dealers, corporate clients, and non-credit organisations.

The spokesperson also highlighted that in late December 2017, the NSD launched the new 'Liquidity Management' service intended to automate money transfers between clients' trading bank accounts for clearing of trades by NSD or National Clearing Centre (NCC), making it possible to regularly transfer cash liquidity to NCC's clearing bank account by using the clearing participant's settlement code.

"The new service allows clients to reduce their costs associated with the management of cash positions at NSD and National Clearing Centre clearing houses. As part of the efforts to harmonise services and to make an integrated value proposition to Moscow Exchange Group's clients, NSD has decided to apply the group-wide approach to the pricing of collateral management and repo trade clearing services", the NSD said.

"From the beginning of 2018, clients are able to benefit from their preferred pricing plan offered by Moscow Exchange for trades involving the use of CMS. The Moscow Exchange Group intends to further develop NSD's CMS for on-exchange and OTC repo and derivatives trades."

Robust and attractive

In 2016, Russia's NSD had a busy year making its securities finance market more robust and attractive to outside investors, and according to the NSD, the volume of assets serviced by NSD surged 55 percent—from RUB 27 trillion (\$411 billion) to RUB 44 trillion (\$670 billion) over the period of four years (2014 to 2018). The Russian Ministry of Finance has announced their plans to build up internal debt (+5-7 percent of GDP in six years) to ensure funding of development projects.

A spokesperson for the NSD noted that NSD has replaced ICSDs as a common depository with regards to the issuing of MinFin Eurobonds and, starting from 2016, new Eurobonds were issued through NSD as clearing and depository centre.

"We are witnessing growing client demand for both investor CSD services (safekeeping and settlement of foreign securities owned by Russian clients) and issuer CSD services (providing access to the Russian market for foreign investors, bypassing ICSDs)", the spokesperson said.

They added: "Regulatory efforts focused on financial market growth and attraction of financial resources from long-term investors and individuals (such as Federal Loan Bonds (OFZ) for retail investors, Individual Pension Capital project, marketplaces, and digital

economy) contribute to the evolution and greater stability of the domestic market.”

“National services providers receive an extra incentive and gain opportunities for growing their business. NSD, which, in addition to a business-to-business model, is developing a business-to-consumer model, is a good example.”

To innovation and beyond

The importance of innovation is a widely spread topic in the industry, and currently the NSD is working on the development of blockchain-based platforms for e-voting, settlement of trades in commercial papers, and record keeping of digital assets resulting from initial coin offerings (ICOs).

Discussing the blockchain platform, NSD explained that: “There are currently two business cases for NSD and blockchain: shareholder voting and commercial papers. In 2017, NSD presented a settlement platform for the issuance of commercial papers by a major mobile network operator.”

“As part of the project, the challenges of ensuring confidentiality of data regarding securities balances and ensuring compliance with specific requirements of Russian laws were successfully solved. A bit earlier, an e-voting system prototype for bondholders was rolled out.”

“In 2018, NSD and Sberbank CIB, a corporate investment banking arm of Sberbank, announced their intention to jointly test the ICO blockchain-based technology through the Bank of Russia’s regulatory sandbox.”

The NSD added: “Testing the pilot project through the regulatory sandbox will allow us to assess the specifics of such transactions, minimise related risks, and receive feedback from the Bank of Russia as to how to improve the mechanisms of those transactions. Our plans are to actively develop the technology, but this would only be possible if the required laws and regulations are in place.”

“We believe it is crucial to lay down a common regulatory framework for distributed ledger technology across all sectors. We are actively cooperating with the regulator in various working groups. NSD has established the CSD Working Group on distributed ledger technology (DLT) to work on requirements and standards and shape best practices in order to make reliable the process of assets movements within DLT-based networks.”

Discussing goals and priorities, the NSD said: “We are moving step by step, building expertise and demonstrating to the market the long-term benefits of the new technology. Our goal is to scale up the technology for various financial transactions and processes. One of the priorities is to reduce the cost of transactions for all players through greater volumes of transactions and involvement of a wide range of issuers and investors.”

Meanwhile, in terms of opportunities and challenges, NSD noted that financial technology will inevitably change of the business model of many companies, whether that be retail, banking or infrastructure business, including the CSD.

A spokesperson for the NSD said: “The most obvious trends are the regulators’ initiatives in the field of collection and analysis of market big data, the use of artificial intelligence and blockchain, and service providers’ efforts to bring together the internet, banking services, social media, and financial technology solutions to create a single data stream for market analysis and launch of new products for clients.”

“Robotisation is in the focus of the financial sector, while active digitalisation entails irreversible qualitative changes in the corporate culture of businesses. A keen interest industry players have in digital assets gives rise to the demand for custody services for such assets.”

“We at NSD are actively involved in so-called digital transformation: we analyse new technology emerging in the market, assess its potential impact on us in terms of both opportunities and threats, and decide on our further steps.”

NSD added: “The financial sector today is a cyberspace, with processes transitioning online, and there is no doubt that the trend will continue. Some companies would be able to adapt and add value to clients, while others will have to leave.”



**Robotisation is
in the focus of the
financial sector**



Looking to the future, the NSD predicted what they expect to see over the next 12 months: “There is no doubt that technology is transforming the role of market infrastructure. For us at NSD, the ultimate goal is to lay down a foundation for the development of the digital economy in Russia and to ensure emergence of a new asset class for investors, as well as ecosystems for ICOs and digital assets trading in the secondary market”.

“Together with the market leaders, we are working on the project to build settlement infrastructure for digital assets, which is an essential prerequisite for institutional investors to enter the market and for ensuring its dynamic development and capitalisation growth.” **SLT**

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Insurance—bridging the gap in securities lending indemnification?

Alan Ball of Texel Finance explains how insurance can be used to bridge the gap between agent lenders and their clients with relation to securities lending indemnification

Justin Lawson reports

Can you give a little detail on your background and experience in this area?

I started my career as a corporate finance lawyer advising clients on a range of capital markets, mergers and acquisitions, and structured finance transactions. After a number of years as a lawyer, I moved across to the insurance industry as an underwriter, leading a niche

team that focused on structuring and underwriting insurance solutions for specialist financial risks. We worked with a range of institutions, including banks and asset managers to provide insurance solutions for risk mitigation, regulatory capital and balance sheet management purposes. The solutions we underwrote included covering securities lending indemnification.

I recently joined Texel Finance, a specialist insurance broker for financial risks in order to grow the market, both among clients and the insurance market for the types of cover that I previously underwrote, including securities lending cover.

How can insurance be used in the context of securities lending indemnification?

Insurance in this context can be used to provide protection against the default of a borrower or repo counterparty—usually in connection with an insolvency event. Exactly how the insurance is used and structured depends on the needs of the insured.

In the simplest structure, an insurance policy is used to indemnify an agent lender against loss they suffer because of a borrower defaulting on a lending or repo transaction. The agent still provides an indemnity to their client but the insurance policy effectively acts as a backstop or counter-indemnity should the agent's indemnification of the client be called if a borrower or counterparty defaults. Cover can be provided by large well-rated insurance companies and so this structure is attractive where the agent doesn't have the balance sheet to efficiently support the indemnity or when the agent's clients want an extra layer of 'sleep easy' protection.

I've also explored using insurance to completely replace the indemnity provided by the agent in respect of borrower defaults. This structure can be logistically and contractually more complicated but has the benefit of completely removing the indemnity for an agent lender, which can help from a balance sheet and regulatory capital perspective. That said, this is something I know is being looked at both by lenders (for their own account) as well as agents.

So can insurance effectively be used to replace the agent lender indemnity?

It depends on the terms of the indemnity you want to replace. If the indemnity is a blanket indemnity, which promises to make the client whole for any loss arising for any reason whatsoever, then that will obviously be a challenge.

However, if a client wants to replace an indemnity and the primary value of the indemnity is in the protection it provides against counterparty default, then insurance can certainly be a replacement solution.

Can you elaborate on what the terms of a typical insurance policy look like in this space?

This isn't an 'off the shelf' product so policies are typically bespoke, being tailored according to the client's needs as well as the requirements of the insurers.

In general terms however, every insurance policy will clearly define the nature and scope of the loss to be covered and include provisions setting out how that loss is to be calculated—these provisions may mirror the standard terms of the underlying trade documents to avoid any basis risk.

The policy will also specify those borrowers and counterparties whose default is to be covered by the insurer and may include a mechanism for adding new counterparty exposures to the cover on an ongoing basis.

A key source of comfort for insurers underwriting the risk will be the risk management practices and track record of the client, so the policy will usually include some representations and undertakings to ensure that key risk management practices continue to be observed. It should be noted, however, that these will be drafted to avoid interfering with or imposing any burden on how the client runs their business—in fact how clients run their business and manage their portfolios can play a big part in getting insurers comfortable with the risk.

The policy will also include a list of exclusions setting out matters excluded from cover. These are usually reasonable and within the controlled of the insured and may, for example, exclude loss arising from a material breach of the underlying lending or repo documents by the insured.

Other key terms are the limit of liability and the tenor of the policy. These can vary depending on the client's needs.

Limits are typically sized by reference to the typical exposure values of the positions in a programme.

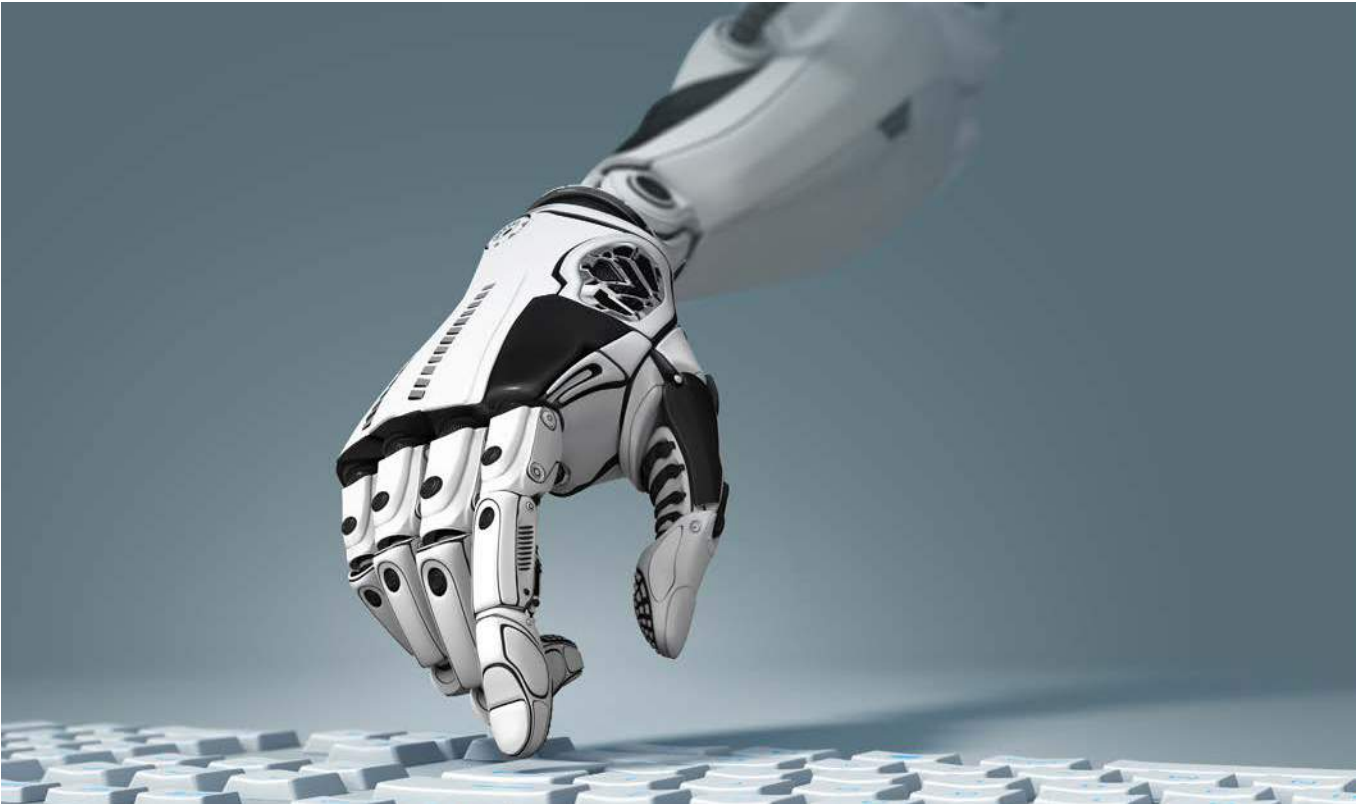
Policy tenors can range from a rolling 12 month period up to 3 years. Longer tenors may be possible but will very much depend on the particular fact pattern in question.

How much does this insurance typically cost?

Premiums for such policies are usually calculated as a percentage of the limit of liability and can range from around 1 percent to 2.5 percent per annum. The actual amount depends a lot on the credit quality of the counterparties to be covered and other policy terms.

Are there any typical hurdles or challenges you've encountered with using insurance in this space?

While securities lending indemnification exposure is covered in the insurance market and there is a growing market appetite for new forms of credit exposure, securities lending indemnification cover is still considered somewhat specialist. It's therefore important to work with parties who are familiar with this sector and who can articulate the risk to the insurance market. [SLT](#)



All about AI

Matthew Battaini of Helix discusses the company's efforts in the industry and the future of technology

Jenna Lomax reports

What trends are you currently seeing in the industry? Is it all regulation?

On the European side, most of the trends have been related to regulation from the Securities Financing Transactions Regulation (SFTR), to the refining of the second Markets in Financial Instruments Directive (MiFID II) requirements or processes.

Although some on the US side have to adhere to the rules of SFTR and MiFID II, one of the regulations we're still hearing about is Rule 204. There are still several firms that aren't in compliance with it, or they outsourced their compliance and they're still having issues with it.

We have geared our Helix applications to help manage the Rule 204 processes.

Another trend is equity for equity trading, this has grown over the past couple of years. We have geared HelixSL to handle the trading

and tracking of "e for e" transactions, as well as added risk-based controls for monitoring balances and collateral schedules/types per client.

How has HelixSL gone since its launch? What have been the most significant challenges and successes?

It's gone very well. We began the development of the product about five years ago. It's been marketed for around four years and its growth has been progressive.

Anytime you introduce a new product in to a mature product space, especially a product space that's been around for 30 years, you need to have a solid core group of development and support, which Helix has.

We also have great stock loan experts and we have more than twenty years' experience in the securities lending space. We started out with one customer and now we have a large customer base, both in the US and Canada—we provide a lot of value for our customers.

Where are you finding the most appetite for your systems coming from?

We see it within the entire range of potential customers. HelixSL has been getting a lot of traction with small-mid size broker-dealers. That's typically the size of client that we generally look for.

How competitive is the technology space around securities finance?

It's extremely competitive. But it creates an interesting opportunity for new vendors, because your large vendors want to do everything for you, but they don't necessarily do everything well. When you're a new vendor, you don't necessarily need to be the master of everything out there, you can pick and choose what you're going to provide in terms of automation and what portions of the office you will cover, for example, front, middle, or back.

What vendors can offer today has come into this space. You get to focus on just being a trading platform, or solely concentrating on regulatory needs. Your customers have such a wide choice of service providers to choose from.

Everyone works well together in this space, meaning if we need to integrate with another platform, people are usually very receptive to that. It's really an interesting time to be in securities finance, especially on the vendor side. As more people get introduced to it, it can only become a better opportunity for the customer.

Where do you see the future of securities finance heading with so much talk around AI, robotics and blockchain?

Well, 2017 to 2018 was the year of blockchain hype. There was a mad dash to become the first company to build a platform and to utilise the technology, even though there wasn't really a need.

I've been in this business for 22 years, since 1996, and when I first heard of blockchain, I thought there would be a five to 10-year integration, just because that's the way technologies work in finance, especially on the post-trade side.

It's apparent on the post-trade side because you must deal with legacy system integrations and, like everything else, this takes time and that's why regulators want to have a say in that.

The blockchain integration craze blew me away because it happened almost overnight. I don't know if I see this same level of blockchain integration within trading. It could be used more within the realms of regulatory compliance, such as improving audit trails, for example.

Now the two topics, robotics and artificial intelligence (AI), are going to heavily play into securities finance in the near future. I know when I say "robotics" you're thinking robots, however robotics in finance refers to robotic process automation (RPA). This will replace a lot of repetitive and user-error prone tasks in the near future, which will not necessarily reduce the workforce but allow it to concentrate on tasks that can reduce loss and increase profit.

AI is another hot topic. AI is something I went to school for. RPA will require some AI, but I see the real tasks AI being applied to are automation for traders, examples of this are automation to identify opportunities or optimise collateral with counterparties.

Everyone loves to throw around the term 'AI', but the definition of AI is the simulation of the human brain by artificial neural networks. That's not what anyone is building here, I guarantee it. What they're referring to is integration of machine learning and data science in to existing platforms. And that's what we'll see developing.

What's next for HelixSL?

We are currently focusing on our North American rollout, although we can support international securities lending desks at this time. We prefer these relationships develop organically by either word of mouth or sales leads from a current customer. However, in saying that we plan to start marketing to European firms later next year.

As we continue to grow, we're still going to maintain our values of great customer service, excellent technology, and always listening to the needs of our customers. We feel these three attributes will carry HelixSL into the future. [SLT](#)



As we continue to grow, we're still going to maintain our values of great customer service, excellent technology, and always listening to the needs of our customers



Matthew Battaini
Director, securities lending product management
Helix

The lending opportunity in CYBG

Sam Pierson of IHS Markit discusses how CYBG's acquisition agreement with Virgin Money created an excellent opportunity for shareholders

- CYBG delivered \$5.9 million in Q3 lending revenue
- Share price has declined 28 percent from a year-to-date peak on 8 August
- Meanwhile, shares on loan have decreased 58% since share price peak
- Merger activity and negative sentiment combine for an excellent lending opportunity

When CYBG announced an acquisition agreement with Virgin Money on 18 June it created an excellent opportunity for long-term CYBG shareholders who were willing to lend their shares. It also created an opportunity for arbitrageurs to profit on the collapse of the spread between the offer price, 1.2125 shares of CYBG per share of Virgin Money, with the initial offer implying a 6 percent premium to the price where Virgin Money shares were trading when the offer was formalised.

CYBG announced their intention to make an offer for Virgin Money in early May, at the time being granted until 4 June to formalise an offer. When CYBG issued a statement regarding the potential offer on 4 June, which announced an extension to the previous deadline, it was taken as an indication that a formal offer was forthcoming. The arbitrageurs jumped on the opportunity, adding more than 30 million shares to the short position in the subsequent three days. The spread narrowed slightly in the following days but remained in the 4.5 to 5.5 percent range until the deal summation came into sight in early September.

Lenders started to increase borrow fees on the initial surge in demand in mid-June, with borrow rates moving north of 250 basis points in late June, coinciding with the utilisation of lendable shares increasing to above 75 percent. With borrow demand increasing past 100 million shares in mid-August, the fees demanded by lenders continued to increase, topping out in the low double-digits for new borrows on 12 September, with utilisation at 95 percent.

The increase in fees came at the expense of the arbs, who must pay the borrow fee to remain in the trade. The peak fee observation immediately preceded the decline in borrow demand, with some combination of arbs and outright shorts deciding to start covering in late September, as the deal spread declined to just over 2%, and the price of CYBG itself declined 8% from the YTD peak.

The spread between the offer price and the price of Virgin Money in daily trading continued to narrow heading into the closing date on 12 October, and briefly inverted on 5 October. The narrowing of the spread prompted some intrepid short sellers to short Virgin Money as well, with the short position in that stock increasing from virtually

nothing on 20 September to 19 million shares on 12 October. That trade worked as well, with the declining CYBG price weighing on the final value of the offer.

And a final farewell to directional short sellers and arbitrageurs has come in the form of the sell-off over the last two weeks of October, which has seen CYBG shares trade down 8.8 percent following the close of the acquisition on 12 October. All told the merger arbitrage would have yielded 5 percent depending on exact entry and exit, while being short CYBG from the announcement of 4 June would have yielded a return of 9.8 percent. In both cases, those numbers are gross of borrow fees, which would have offset the return by 170 basis points in realised borrow fees during that time.

The corollary is true for CYBG shareholders, who have seen a corresponding boost in the form of lending revenue. They also saw the value of their shares decline over the past six months, however, the decline in valuation for CYBG was similar to the major UK equity indices over that span, a broad holding of which would have delivered far less in realised lending revenue. [SLT](#)

CYBG Pic equity short demand & share price



Virgin Money Holding (UK) Pic equity short demand & share price





Appointments at Broadridge and J.P Morgan

Broadridge has appointed Tom Carey as president of global technology and operations (GTO).

In his new role, Carey will oversee the growth of Broadridge's core technology business globally across capital markets, wealth, and investment management.

Carey will also continue to oversee Broadridge International until a new leader is formally appointed.

Meanwhile, Charlie Marchesani, former president of GTO, will serve as strategic advisor for the segment's critical growth themes including strategy, merger and acquisition, and product management.

Previously president of Broadridge International, Carey reports directly to Tim Gokey, who will become CEO of Broadridge's core technology business globally across capital markets, wealth and investment management.

A 25-year veteran, Carey led the combination of all of Broadridge's international business into a single integrated unit earlier this year to bring Broadridge's full scale to global client solutions.

Previously, he led the company's technology and operations solutions in Europe, Middle East, and Asia, and Asia Pacific for nearly a decade.

Gokey commented: "Tom Carey is an incredibly capable, technology-focused industry executive. He has driven the growth of our global capital markets business and, more recently, our overall international portfolio."

"We see the continued mutualisation of technology and technology innovation as the future of the industry, and Carey is the right leader to bring the next generation of technology including artificial intelligence, blockchain, cloud, and digital to our capital markets and wealth and investment management clients globally."

Carey added: "Broadridge has consistently delivered scalable and proven technology and operations solutions to help clients transform while gaining significant cost efficiency. Looking ahead, we aim to accelerate this pace of change on a global scale."

"We are uniquely positioned to help clients get ready for what's next by providing the on-ramp to the next generation technology

and innovation to help them meet their growth objectives."

J.P. Morgan has appointed Bhavna Haswani as senior product manager.

Haswani will report to O'Delle Burke, head of collateral management products for Asia Pacific.

Based in Hong Kong, Haswani will be responsible for triparty collateral management and Asia Pacific product initiatives.

Haswani has more than 10 years of experience within securities lending and collateral management.

She has held senior roles at BNY Mellon, Deutsche Bank and Barclays Capital.

Haswani's appointment follows the recent hires of Yan Xu, covering product development and derivative collateral management in the region and Rikako Uehara, who is responsible for collateral management in Japan.

Commenting on Haswani's appointment, Burke said: "I'm delighted with the ongoing expansion of our product team demonstrating commitment to build our franchise in the region." **SLT**