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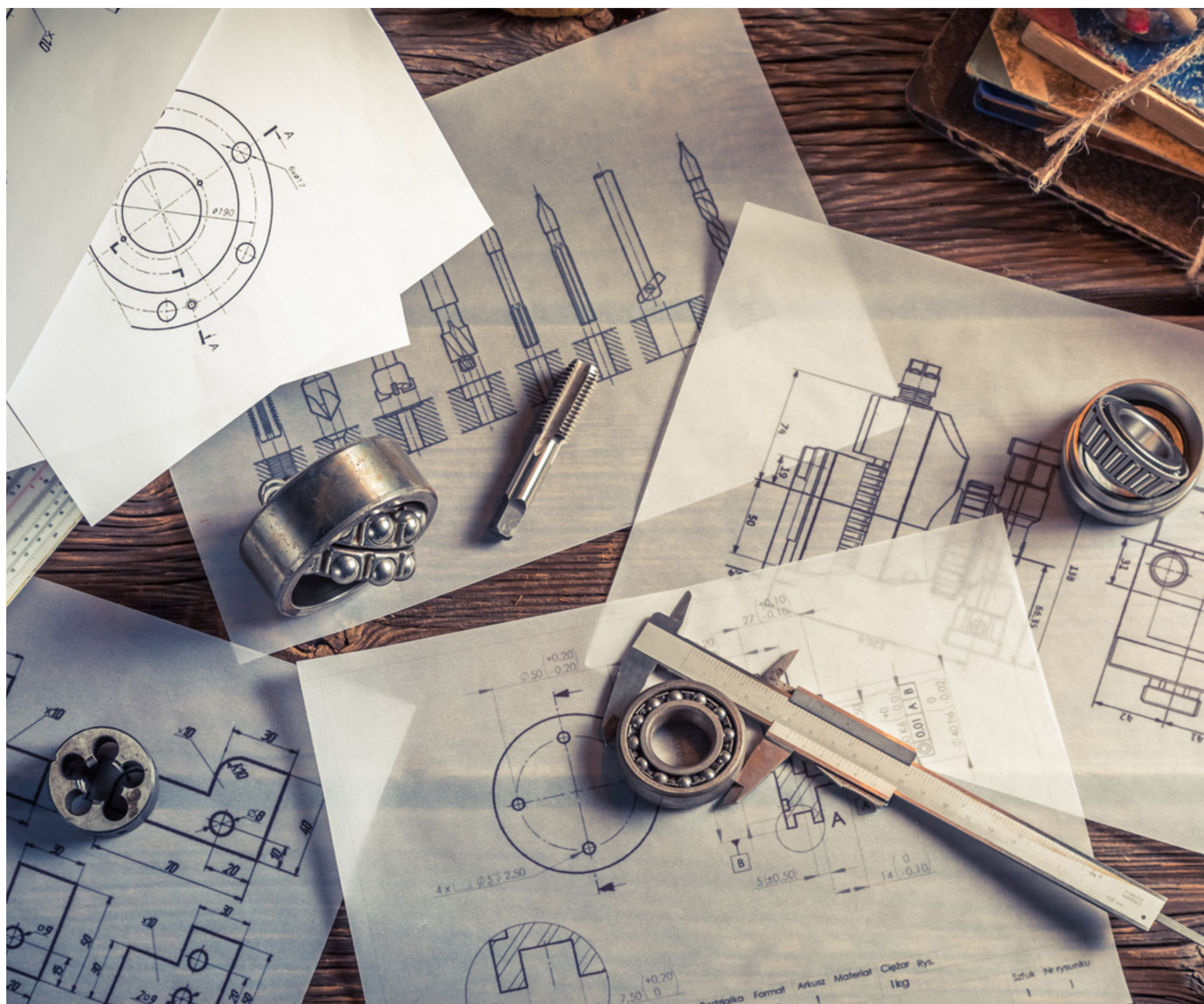

SFTR XML schemas arrive late and defective

The European Securities and Markets Authority (ESMA) has belatedly published the third draft of its XML schemas for reporting transactions under the Securities Financing Transactions Regulation (SFTR), but further guidance will be needed to resolve known defects before the April 2020 deadline, according to industry sources.

Market players are now concerned that SFTR will suffer from the same reporting issues that plagued the European Market Infrastructure Regulation (EMIR) and the Markets in Financial Instruments Regulation (MiFIR) when they first came into force.

The timeline for developing each draft of the SFTR XML schemas is understood to have been hampered by several delays which meant that the ISO 20022 Securities Standards Evaluation Group's evaluation team (ET), which is responsible for reviewing and approving ESMA's submission for SFTR messages, was not given enough time to raise and resolve concerns before the third draft was published.

In two meetings between ESMA and the ET following the submission of the third draft in mid-October, multiple defects were highlighted by the ET, including in a meeting on 31 October. These concerns were acknowledged by ESMA at the time but were not enough to delay the draft's pre-arranged publication later that same day.

The primary consequence of this is that the common XML templates are not ISO-registered, which was widely understood to be the required standard as laid out in level two text of SFTR. An explanatory note attached to the third draft release described the schemas as being in accordance with ISO but did not claim it was or would be stamped as such.

An industry source with knowledge of the matter, who wished to remain anonymous,

Continued on page 6

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Latest News

Deutsche Bank's former global head of agency lending, Tim Smollen, is understood to be taking on a leading role at MUFG investor services

page 6

Malik's Memo

Seb Malik of Market FinReg lays out the case for regulators to take large institutions to task over IT failures

page 12

Country Profile

India's securities lending market continues to grow, but what should the country do to maintain momentum?

page 13

Regulation Riposte

Deutsche Boerse has responded to the threat of CSDR's mandatory settlement requirements a with a new buy-in service

page 15

TR Update

UnaVista's Catherine Talks, discusses how the LSEG is offering compatible solutions to help the market get ready for SFTR

page 18

Data Analysis

David Lewis of FIS surveys the state-of-play for the industry in the final run up to SFTR and notes the many hurdles yet to be cleared

page 21

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SFTR XML schemas arrives late and defective

continued from page 3

said that the ISO registration process is understood to still be underway. ESMA is expected to submit a fourth XML draft to the ET on 15 November, which will then be given implicit ISO approval if no further concerns are raised by 22 November.

Tomas Bremin, convenor of the ISO ET and vice president of REGIS-TR, explained that the team's latest findings were that workarounds will be needed if securities finance market participants are to use the current third draft as a reporting framework.

"We are looking forward to ESMA's guidelines in this regard," he said, adding that the ET had concluded its 10th meeting with ESMA last week and that a fourth draft would be required to formally achieve ISO registration.

"As convenor of the ISO ET assembled to review and approve ESMA's submission to ISO 20022 of SFTR messages, I salute the team's accomplishments in gaining numerous and significant improvements to March's draft-two submission on behalf of market participants," Bremin continued.

However, multiple industry figures are now voicing concerns around the costs and challenges that will arise from the need for further amendments to the reporting templates to resolve defects known today, along with others expected to be revealed once reporting begins.

Reacting to the delayed XML release, Matt Smith, CEO of SteelEye, a London-based regtech and data analytics provider, said: "The fact of the matter is, we are six months before the regulation goes live and they only just released the XML format, and there is still a lot of room for interpretation."

"We continuously see the regulator not understanding things and leaving things very late. Six months is not a lot of time to have the XML fully standardised," he noted. "People need to build their reporting capabilities and test them and go through validation and to say that everyone is going to do that when they were only just released is impractical."

"The regulators are as under prepared as the market. I think we will see huge amounts of teething issues and it could take six months to a year before things are flowing well."

However, Smith went on to note that those in-scope for SFTR have had more time to prepare this time around, compared to previous regulatory frameworks. He added that the work already put into reporting requirements for EMIR and MiFIR would be a stepping stone that makes preparations for SFTR easier.

ESMA declined to comment on the XML schemas.

Deutsche Bank's agency lending team heads to MUFG

Deutsche Bank's former global head of agency lending, Tim Smollen, is understood to be taking on a leading role at Mitsubishi UFJ Financial Group's (MUFG) investor services division in January to grow its securities finance business, as part of a wider strategy to grow the Japanese banking group's global presence.

For Deutsche Bank, Smollen was based in New York but it is currently unknown whether he will relocate for his new role or if it will be global or regional in scope.

It is believed Smollen will be joined at MUFG by fellow Deutsche Bank alumni Jay Schreyer and Anthony Toscano, who also left the German bank recently, among others.

At Deutsche Bank, Schreyer served as head of agency lending for Europe, the Middle East and Africa (EMEA), and Asia Pacific, while Toscano was co-head of agency lending for North America.

The trio has maintained a professional partnership on-and-off for over a decade, having first joined forces to develop Dresdner Bank's securities lending business in the early 2000s, before it was acquired by Commerzbank in 2009 for €9.8 billion.

They later joined forces again at Deutsche Bank in 2009 to develop its agency lending business following the financial crisis, where the bank suffered worse than most.

It is now understood that the team will bring their experience to bear on MUFG's securities lending programme, which has been active for more than 20 years already under the umbrella of its investor services arm.

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Other recently departed members of Deutsche Bank's global agency lending desk are also expected to re-appear at MUFG.

MUFG's securities lending hires are only the latest in a series of key senior appointments in a wide variety of market sectors in the past 12 months, which were all cited as being aimed at achieving the bank's growth targets across all global regions.

MUFG boasts a global network of entities in more than 50 countries, which it aims to leverage to cement its position as a leader in multiple financial markets, including securities lending.

MUFG were unable to immediately offer a comment on the agency lending hires.

LEIs could conjure up cost benefits, says McKinsey & Company

Banks could recoup some of the costs of creating legal entity identifiers (LEIs) under Securities Financing Transactions Regulation (SFTR) with operation cost savings elsewhere, according to a new market whitepaper.

The report by McKinsey & Company, in partnership with the Global Legal Entity Identifier Foundation, claims that savings of "at least 10 percent of total operations costs for client onboarding and trading processing for banks adopting the LEI are possible".

An LEI is a unique code that identifies legal entities participating in financial transactions and is required by firms to fulfill their regulatory reporting obligations.

LEIs are already required under the European Market Infrastructure Regulation (EMIR) and the Markets in Financial Instruments Directive (MiFID), as well as being a key component of the EU's SFTR, which is due to come into force in April 2020.

The report, entitled 'The Legal Entity Identifier: The Value of Unique Counterparty ID', emphasised that the LEI's primary value, other than being required by market regulations, is derived from reducing the cost of onboarding clients and of middle- and back-office activities related to the processing of stocks, bonds, and other securities trades.

According to the report, the operational costs savings could amount to $150 million annually for the broader investment banking industry.

Commenting on the whitepaper, Simon Wood, CEO at Ubisecure, a software company, highlighted that LEIs connect the many pieces of reference data for processes related to know-your-customer (KYC) and anti-money laundering (AML) rules.

"In most cases, different areas in the lender use different identifiers for the same client – and that makes what should be a simple task becomes very complex and expensive," he added.

"The LEI enables cost-reduction by making the reference data standardised and readily available during both the initial KYC process and then the ongoing identification of counterparties as trades occur."

The whitepaper's findings will be welcome news for many in the securities financing industry, who are in the midst of building LEIs into their transactions ahead of SFTR's go-live. The LEI requirement of SFTR is often cited as one of the more burdensome features of the regulation due to its complexity and the cost of the technical build, compared to existing rules frameworks.

SFTR reporting requirements mandates 155 data fields, compared to 129 required under EMIR for over-the-counter derivatives.

Elsewhere, the International Securities Lending Association (ISLA) has repeatedly warned that the consequence of some market players not having their LEIs in place would be a drain on overall liquidity as they would be unable to transact in the securities finance markets once SFTR is live.

In September ISLA warned that "considerable effort" is still required to improve asset issuer registration for LEIs to meet the requirements of SFTR.

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ISLA's market research, along with others, has shown that European market participants are well on their way to having LEIs in place for their securities finance transactions but that non-EU entities that will not directly be in-scope for SFTR are lagging behind in their preparations. This will create complications down the road as the regulation's reporting requirements include transactions data from non-EU counterparts.

Phillip Morgan, COO and head of sales at Pirum, explained that coverage of LEIs within the EU is relatively high, driven by existing reporting regimes, such as EMIR and the MiFID, while adoption rates outside of the EU remain at lower levels.

"This will present challenges for institutions required to report an issuer LEI as part of their overall SFTR reporting requirement, especially as most firms transact and receive collateral in assets issued both within and outside of the EU," he explained.

"We're working to support our clients with the sourcing of issuer LEIs when they are available and at the same time we're also working with the trade association working groups to help highlight some of these challenges to the regulators and propose alternative, practical approaches."

Euroclear Finland to join T2S in 2022

Euroclear Finland is set to join the European securities settlement platform TARGET2-Securities (T2S) in November 2022.

T2S aims to offer a centralised delivery-versus-payment settlement in central bank funds across the European securities market.

The timing of Euroclear's connection to T2S will coincide with the launch of European Collateral Management System (ECMS), ensuring that access to collateral eligible securities in Euroclear Finland's safekeeping continues.

In addition, Euroclear Finland deployed its new CSD system, Infinity, in May 2018. Then in August, Euroclear Finland was given the green light to operate under the EU's Central Securities Depositories Regulation (CSDR).

The most recent new features of Infinity include Partial Settlement, introduced in September 2019, and Equity Savings Accounts, which will become available for retail investors in Finland in January 2020.

Hanna Vainio, CEO of Euroclear Finland, said: "The roadmap of joining T2S has been agreed in close collaboration with market participants, Bank of Finland and the European Central Bank."

She added: "Just like in the previous stages of the Infinity programme, we will work together with clients to ensure a smooth transition

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IHS Markit and Pirum Systems adds UTI sharing service to SFTR solution

IHS Markit and Pirum Systems have added a unique trade identifier (UTI) sharing system for third-party firms to their joint-Securities Financing Transactions Regulation (SFTR) solution.

The service – UTI Connect – is designed to support industry best practices by exchanging UTIs and other information with financial market intermediaries or counterparties that are not leveraging the SFTR solution.

According to Pirum, the joint-SFTR solution provides the market with comprehensive coverage for data sharing, including UTI and agent allocation information.

In a statement on the UTI service launch, Pirum said that more than 60 firms have committed to using the platform, and they are now bilaterally testing its end-to-end services, including transaction and collateral reconciliation and reporting using ISO 20022 (XML) standard messaging.

According to Pirum, its network provides connectivity to 14 of the top 15 brokers, 13 of the top 15 lenders, and 80 percent of the industry's trade volume available for pre-reconciliation, UTI sharing and other data required for SFTR.

Among other participants, the network provides connectivity to 80 percent of the industry's trade volume available for pre-reconciliation, UTI sharing, and other data required for SFTR.

Pirum's head of SFTR, Duncan Carpenter, observed: "From inception, we have always planned to support firms that need to connect to those not on the platform and have been working closely with our clients and industry bodies to define how the process will work."

"We are pleased to confirm we have reached working agreements with other vendors that are also supporting UTI sharing."

Pierre Khemdoudi, managing director and global co-head of equities, data and analytics at IHS Markit, added: "As we learned with EMIR, UTI sharing can be a major challenge for firms and regulators as they aim to get a meaningful view of all the data submitted to trade repositories."

Khemdoudi added that IHS Markit is working in close collaboration with the industry to simplify information sharing workflows and increase matching rates.

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in April 2020 and will require banks and investment firms to report their securities financing transactions for the first time.

EquiLend sets deadline for SFTR solution sign-up

EquiLend has warned prospective users of its Securities Financing Transactions Regulation (SFTR) reporting service that they must commit to its solution by 15 November in order to be fully prepared for the regulation's go-live in April 2020.

SFTR will require banks and investment firms to report securities financing transactions to a registered trade repository for the first time.

In an email to clients, EquiLend outlined that those who miss next week's deadline risk missing out on its "premium on-boarding experience," which includes the attention of dedicated specialists who will coordinate front-to-back testing; detailed scenario testing; user acceptance testing; and access to the EquiLend Lab to facilitate bilateral testing.

Elsewhere in the note, EquiLend acknowledged that clients are already well underway on testing its solution.

In a separate blog post on the firm's SFTR solution, EquiLend's vice president of post trade, Mark Byrne, said that its SFTR build has been designed to facilitate the deployment of functionality in a modular, flexible manner, which allows client firms to build out at their own pace.

"This in turn means EquiLend is poised and ready to meet changing client needs and offer efficiency, transparency and control across an ever-expanding suite of industry-leading products and services," he added.

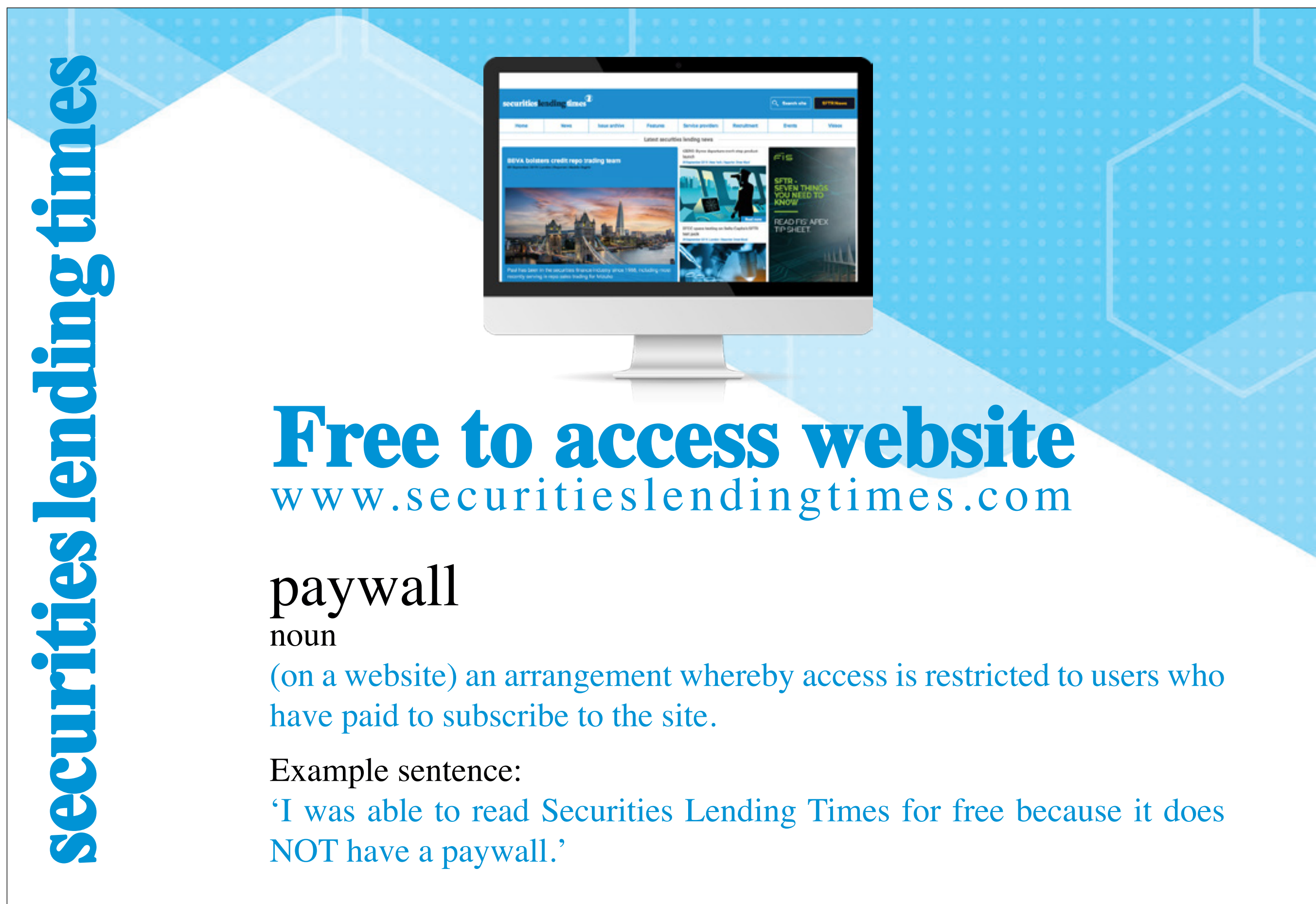
deltaconX partners with KRM22

The regulatory reporting service, deltaconX, that helps market participants meet regulations such as the Securities Financing Transactions Regulation (SFTR) has partnered with KRM22.

KRM22 will utilise deltaconX's solution, a service-based platform, which will be available through KRM22's global risk platform.

The platform enables firms to meet regulatory reporting requirements including European Market Infrastructure Regulation, and the second Markets in Financial Instruments Directive, as well as SFTR.

According to KRM22, the application simplifies the reporting process through automation and error handling, minimising manual work and the likelihood of human error.



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Regulators encouraged to act against IT failures

The UK Parliament's Treasury Select Committee released a much-anticipated report entitled 'IT failures in the financial sector' in late October. I wholeheartedly welcome this report's recommendations. IT systems are relied upon like never before in the financial sector.

The committee accepts that "uninterrupted access…is not achievable" yet cautions that "prolonged IT failures should not be tolerated".

The committee considers it crucial for regulators to intervene to "not allow firms to set their own tolerance levels for disruption too high".

This is important because, under English contract law, business-to-business contracts are not afforded consumer protections such as unfair terms or cooling-off periods.

If an individual engages in a contract with a business, unfair terms will be struck out, irrespective of the consumer signing a contact, eloquently put by Lord Denning in (Chesterhall) v Finney Lock Seeds:

"None of you nowadays will remember the trouble we had - when I was called to the bar - with exemption clauses. They were printed in small print on the back of tickets and order forms and invoices. They were contained in catalogues or timetables. They were held to be binding on any person who took them without objection. No one ever did object. He never read them or knew what was in them. No matter how unreasonable they were, he was bound. All this was done in the name of 'freedom of contract'."

"But, the freedom was all on the side of the big concern which had the use of the printing press. No freedom for the little man who took the ticket or order form or invoice. The big concern said: "Take it or leave it."

"The little man had no option but to take it. The big concern could and did exempt itself from liability in its own interest without regard to the little man. It got away with it time after time. When the courts said to the big concern: "You must put it in clear words," the big concern had no hesitation in doing so. It knew well that the little man would never read the exemption clauses or understand them. It was a bleak winter for our law of contract."

Yet these protections do not apply to business-to-business contracts. I work for a firm much smaller in size than the celebrated financial behemoths that we engage with. We are regularly presented with manifestly unfair contracts with unfair service-level agreements. The contracts are presented in a 'take-it-or-leave-it' manner. Our bargaining power is precisely zero. And so we, and thousands of small-and-medium enterprises like us, sign on the dotted line with gritted teeth.

When we encounter failures in service, the behemoths waive the unfair contract in front of us reminding us that we 'agreed' to the terms. Simply stated, there is nothing we can do.

The MP Anna Soubry lobbied to extend consumer protections to small businesses during her time as a business minister but to no avail. It is, for this reason, the latest call for the regulators to act is appreciated.

To be clear, the select committee's report does not address this change in English law but any action that increases accountability and responsibility is to be welcomed.

Banks have been critical of the regulatory burden through excessive demands. The UK's Prudential Regulatory Authority (PRA) has dismissed this criticism. Sam Woods, of the PRA, said: "As is often the case, members of some financial institutions may be expressing themselves more vividly than the facts support." Meanwhile, his colleague Lyndon Melson acknowledged, global banks have been "hit by a variety of different standards".

Business continuity and mitigation of IT failure is set to shoot up in regulators' agendas with the adoption of cloud solutions. Firms seeking to get ahead of the curve should commence analysis now.

Broadridge and SimCorp recently announced their adoption of cloud technology. My firm, Market FinReg, has solutions that use Amazon Web Service cloud technology. Almost all technology providers are either currently transiting to cloud infrastructure, or plan to do so. Avid readers will recall my citing the European Banking Authority's report on outsourcing to the cloud. This week I met deltaconX in Vienna. We both agreed that the future is the cloud and it was question of when, not if, banks signed up.

Regulation is essential to ensure business continuity, resilience, data protection, accountability and the setting of minimum service level agreements.

Seb Malik
Head of financial law
Market FinReg

Building Momentum

India's securities lending market continues to grow, with borrowing volumes hitting record levels in October, but what should the country do to maintain this momentum?

Maddie Saghir reports

India has been hailed as one of the major success stories in Asia by industry experts as the country's securities lending industry has continued to grow in recent years. So far this year India's government and market regulator have been proactive in seeking to encourage market activity and have made several moves to encourage further growth. Their efforts were rewarded in October when the country experienced an all-time high in borrowing volumes, reaching around 30 million shares on loan.

However, challenges still remain. First and foremost, the market is hampered by the fact that it operates via a mandatory central counterparty (CCP) structure that many foreign institutional investors are not currently comfortable with. Further, to this, issues exist with the term requirements, recall process and collateral.

The Reserve Bank of India (RBI) and the Securities and Exchange Board of India (SEBI) have come up with a number of initiatives over the past years in order to overcome these challenges.

In September, RBI deputy governor Shri Kanungo announced that the bank is working with market regulators on a securities lending product to improve India capital market liquidity and avoid a short-squeeze incident.

As well as this, back in January, SEBI notified the market that all derivatives will be settled physically as part of an initiative to help promote securities lending. One of the main objectives of this is to have a better alignment of cash and derivatives segments. At the time, SEBI stated that a "prerequisite for the successful introduction of physical settlement of derivatives is efficient and transparent lending and borrowing mechanism in cash segment".

Discussing how effective SEBI's initiative has been almost a year on, Prem Purohit, senior vice president of securities lending at HSBC Global Banking and Markets, India, says that although it is difficult to quantify the effect and causal relationship on the securities lending market, the lending activities did see positive growth post implementation of physical settlement of derivatives.

Another major factor contributing to the growth, Purohit observes, is policy changes related to treatment of corporate action, such as allowing markets to have securities lending contracts without mandatory foreclosure in event of annual general meetings or extraordinary general meetings. This, he says, has contributed to the expansion in breadth of the market in terms of the variety of stocks being borrowed.

However, despite proposed changes and initiatives, Ed Oliver, managing director, product development at eSecLending, comments: "A SEBI-led workstream made a series of recommendations for updating the securities lending rules a few years ago. Whilst there have been some small changes, there are still fundamental issues that require resolution before widespread foreign participation is likely."

Oliver also noted that the Pan Asia Securities Lending Association is engaging with market members in India to offer its support as required.

"However, at this stage, other markets in Asia, such as Indonesia, the Philippines and China appear to be more engaged on developing both securities lending and short selling markets," he adds.

A rocky ride

Growth could be spurred further if an easier route to market was established as there are still some challenges for foreign institutional investors who want to engage with India. eSecLending's Oliver says: "Issues exist with the term requirements, recall process and collateral. Loans are on a fixed term basis, typically one month to one year, and recall (ahead of the end date of the loan) is on a best efforts basis."

As well as this, Oliver notes, that collateral must be onshore cash only. "The ability to execute loans on an open basis with offshore cash and non-cash collateral would be more attractive to foreign institutional investors, preferably through a bilateral arrangement," he explains.

Currently, to be able to participate in the Indian securities lending market, one needs to go through a registered 'participant', which includes brokers or custodians designated as such in the securities lending segment.

For a registered foreign portfolio investment (FPI), investors have to

execute an agreement (the same way they do for other segments) with the registered participant to engage in India's securities lending market. HSBC's Purohit argues that the challenges for FPIs to participate in India's securities lending are inconsequential and highlights that many foriegn investors are active today in India, but external sources indicate that the barrier to entry is still too high for some.

Yogesh Radke, head of alternative and quantitative research, institutional equities at Edelweiss Securities, outlines that "with respect to the foreign borrows, it is expensive to borrow as the margin requirements are still in the form of Indian rupee (no other cash equivalents are allowed)".

Secondly, Radke notes that the remittance of the funds generated by selling of the borrowed equity needs to be cleared. "Currently, it can't be taken out of the country as tax can't be calculated of the equity sold via borrowing," he explains.

However, Purohit observes that although the expense is an issue, it has been addressed by the RBI. He says: "FPIs now are permitted to offer non-cash collateral (same as applicable in cash and finance and operations segments) for their securities lending trades. So from that sense, I think it is a level playing field for foreign borrowers."

Further to this, in terms of challenges, during a panel at the International Securities Lending Association post trade conference earlier this year, one panellist said that India's securities lending is quite a convoluted marketplace. Of this, Radke notes: "We do believe it is different from the global borrowing and lending mechanism as it is exchange traded and exchange guaranteed platform. SEBI, exchanges and the RBI have to make some changes to make the system more smooth."

Purohit disagrees on India being a convoluted marketplace, however, and argues that securities lending in India, which is exchange traded, may be different from the more common international experience of the over the counter (OTC) model but it is gaining momentum.

"The exchange-traded model has its pros and cons as has the OTC model," He says. "The market is picking up momentum and with increased participation by domestic and cross-border investors, it should further deepen."

When all is said and done, while there is clearly some ongoing challenges in India, the data doesn't lie. Purohit points to the fact that overall, the country's securities lending market is expected to grow by 20 to 25 percent in 2019 over the previous year, which shows that the industry is heading in the right direction.

Dissecting the data

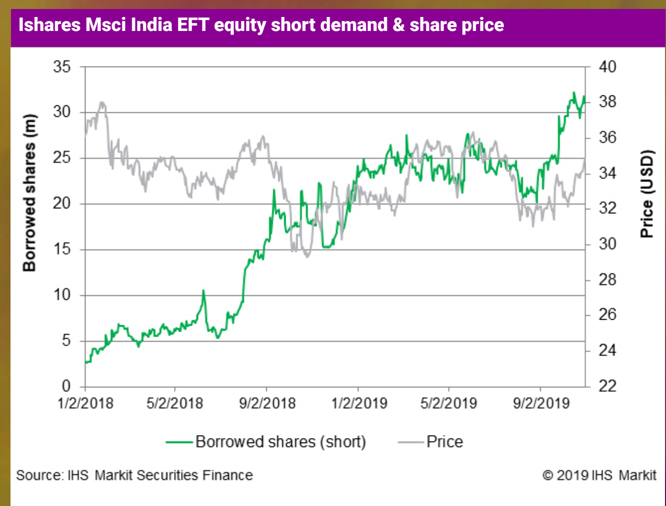
Breaking down the data to see the roots of this growth, Purohit highlights that for 2019, market-wide lending fees stood at approximately US$20 million and the value of lent stocks stood at $3.8 billion till September. This data compares with lending fees of $18 million and $9 million in 2018 and 2017, respectively.

On a macro level, Sam Pierson of IHS Markit says: "Looking at the INDA exchange-traded funds (ETF) (see figure one) we can see an increase in borrowing in recent years to an all-time high in October of 30 million shares (20 percent of shares outstanding)."

The chart shows that the value of the borrowed shares, a proxy for the total short position, reached $1 billion for the first time in October. The ETF currently has $5.2 billion in assets after $360 million in inflows year to date (YTD), while the value of loan has increased by $270 million YTD.

According to Pierson, the spike in shares on loan in late May 2019 coincided with the largest weekly inflow for the ETF, suggesting some of the inflow was creation of ETF units for borrow. Currently, shares of the ETF remain inexpensive to borrow with utilisation at only 50 percent.

Figure 1



So, while the data shows growth in India's securities lending, further work can be done in order to achieve even more opportunities in the country's marketplace, with a focus on making life easier for foreign investors coming near the top of the market's wish list for the coming months and years. Radke notes that once the foreign margin and remittance issue gets ironed out the offshore supply/demand will pick up in India.

In the broader Asian picture India's development is in tandem with many countries in the region that are growing their securities lending market. Earlier this year one industry expert observed that markets across the Asia Pacific region are continuously developing, providing a plethora of growth and revenue optimisation opportunities. As long as India continues to focus on developing their market infrastructure and encouraging participation, the regional tailwinds pushing Asia's growth as a whole will continue to ensure momentum is sustained into 2020 and beyond. SLT

Responding to demand

CSDR represents the first example of legally mandated loan settlements with the added twist of cash penalties for fails. Deutsche Boerse has responded to this threat with the formation of a new buy-in service

Drew Nicol reports

For the securities lending industry, 2020 will be a year of firsts. In April the Securities Financing Transactions Regulation will require a granular level of transaction reporting hitherto unknown in the industry. Beyond that, the Central Securities Depositories Regulation (CSDR) will seek to improve settlement discipline with the introduction of mandatory buy-in rules and even cash penalties for fails, both also industry firsts.

The cash penalties and buy-in requirements for failing transactions kick in at varying dates from the intended settlement date (ISD) depending on the liquidity of the instrument in question–specifically, on ISD+4 for 'liquid' securities and ISD+7 for those deemed illiquid.

In its report on the CSDR's impact on the market (published in February) the International Securities Lending Association (ISLA) did not mince its words when it described the regulation's features as likely to bring additional costs and greater risks and complexities to the market.

The CSDR buy-in provision is slated to come into force on 14 September 2020 and will apply to trading entities domiciled not just in the EU but also the European Economic Area and even beyond.

To put the scope of the potential challenges mandatory buy-ins in context, settlement rates for securities lending transactions in 2018 were estimated to be between 80 percent and 90 percent, with the majority of failed settlements occurring on the return leg of loan transactions, according to ISLA's Q1 2018 report.

However, the good news for the market is that all securities financing transactions with a term of fewer than 30 days will be exempt–a fact which brought an industry-wide sigh of relief when it was first announced.

In theory, this exception grants market participants a fair amount of wiggle room to manage their open transactions accordingly so as to avoid falling foul of buy-ins and penalty rules, but the true impact of CSDR on the market will remain unknown until it is upon us next year.

Given the period of uncertainty within which the market now operates, it will no doubt be a comfort to many that Deutsche Boerse has become the first to throw its hat into the ring to offer a service that directly mitigates the thorny issue of mandated buy-ins. Under the stewardship of Marcel Naas, formally of Eurex Repo, and Marcus Addison, who shifts over from Eurex Clearing, the German exchange has founded a new company that will act as a neutral buy-in agent for the market. The service is on track to launch in September 2020, in time for day one of CSDR's implementation.

To discuss the finer points of what the buy-in agent service can offer the market, SLT sits down with the company's new managing directors.

This is a new venture for you both after many years in other areas of Deutsche Boerse. What can the industry expect?

Marcel Naas: The regulatory framework of CSDR allows for a neutral buy-in agent and we at Deutsche Boerse saw this as a natural progression of our existing services. We already have a lot of experience in settlement and post trade, as well as offering some buy-in services out of our central counterparty (CCP).

As a result, we founded a new company in July called Eurex Securities Transaction Services, which will host the new buy-in service as a subsidiary of Eurex Frankfurt. The service will be launched in September 2020 in time for the new harmonised standards for settlement discipline that come as part of the EU's CSDR.

The service aims to offer Deutsche Boerse customers with a high level of standardisation and automation to resolve the challenges posed by the mandatory buy-in requirements imposed by CSDR. We will require a banking licence for this service and we are currently applying for that with the German Federal Financial Supervisory Authority.

Marcus Addison and I will run the company and we are currently building up a team that will assist us in that aim.

Deutsche Boerse is the first, and only, market participant to embrace this opportunity to become a buy-in agent so far. Why is that?

Marcus Addison: The CSDR rules are quite strict in outlining that a buy-in agent must be neutral in the market. This plays to our strengths as Deutsche Boerse Group does not hold a position on any security.

Naas: This requirement will have limited the number of entities that can take on this mantle of a buy-in agent. More people may come forward as time goes on but at the moment it is only us.

What impact do you expect CSDR to have on the securities finance industry?

Naas: It will have more of an impact on the underlying markets because transactions with terms less than 30 days are excluded. The question is whether that remains the case or if things change over time - nobody knows. At the same time, it may be the case that more people turn to securities lending and repo as a way to avoid settlement fails.

How are buy-ins currently executed and how will that change under CSDR?

Addison: Buy-ins are usually done via a CCP and its safe to assume some buy-ins occur bilaterally as well, although the number of these is hard to quantify. Once CSDR comes into effect buy-ins will be mandated after the trade is deemed to have 'failed' and so that will naturally increase the overall number of buy-ins that are initiated.

Through Eurex Securities, we will run a series of daily over-the-counter auctions to attempt a buy-in for the required securities. We are not a marketplace and we only facilitate an auction for the security to be bought, so that will not always be successful. If it isn't successful then that will be reported to the instructing party and, in those instances, the original transaction will have to be cash-settled as mandated under CSDR.

How many transactions can we expect to run into the buy-in rule?

Addison: Precise data on settlement fails in the securities finance market is hard to come by. Some estimates say that up to 20,000 trades a day fail to settle in Europe, which represents between 2.5 percent and 3 percent of all transactions that take place daily. The question is, how many of those will remain open once the time allowed by CSDR to settle has elapsed, which could be either four, seven or even 15 days depending on the liquidity and type of instrument. At the same time, we expect the industry to engage in efforts to improve its settlement deficiencies so the number of fails will go down.

In terms of buy-in success rates, that will depend on the liquidity of the instrument. That said, CCPs already do buy-ins and I'm sometimes surprised at the types of instruments that go into buy-ins and their success rates, which is relatively high, although that's partly to do with the highly-liquid basket of instruments with which the CCP is active.

By codifying buy-ins in law, do you foresee CSDR providing greater standardisation and best practice in this feature of transactions?

Addison: Today there are some issues in the market because there are disputes around which side of the trade will ultimately pay if a buy-in is instigated. In the future, this will be clear under CSDR as the buyer must instigate the buy-in and the seller must cover all the costs. Even if trade reverts to a cash settlement then CSDR includes a formula for that as well. **SLT**

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Zürcher Kantonalbank

Presenting a united front to SFTR

UnaVista's SFTR product manager, Catherine Talks, discusses how the London Stock Exchange Group has come together to offer compatible solutions to help the market get ready for go-live of SFTR

Maddie Saghir reports

UnaVista recently hosted an SFTR roundtable, what were some of the main takeaways?

At the London Stock Exchange Group, a number of our businesses including UnaVista, LCH and MTS, as well as our clients, are affected by the Securities Financing Transactions Regulation (SFTR). We have come together to offer solutions that are compatible to help the market get ready for reporting in an accurate and consistent manner.

The presentations given at the roundtable looked at the challenges we found talking to our members.

We were also talking about our offerings. LCH is a clearing house and has a reporting obligation, so we have come together to offer what we call 'assisted reporting' for LCH's RepoClear members. We will take LCH's side of the trade and then make it available for the other counterparty so that it helps them know that the reference data is provided from the golden source of the central counterparty (CCP). This will ensure that there will be a good result in the reconciliation process at the trade repository.

We are also working closely with MTS, one of Europe's leading electronic repo platforms. MTS has developed the SFTR blotter, which automatically enriches cleared and bilateral trades on the MTS repo platform with collateral and master agreement reference data and maps these to the SFTR fields and formats. We are working with MTS so that the SFTR blotter can be sent directly to the UnaVista trade repository under our technical router model. This means that the repo market can benefit from straight-through-processing from execution and clearing to reporting.

We are six months away from the implementation of SFTR, will market participants be ready?

The response that we have found has been quite varied. SFTR, unlike other regulations, doesn't just have one start date, it is actually a staggered start date, which means that there are four different phases at which different entities come into scope for reporting. Because of that, depending on the cycle you're obligated to report in, there are different waves and variation in how ready firms are. The European Securities and Markets Authority (ESMA) has published a number of texts for firms to utilise for reporting purposes. The level two text explains what fields have to be reported and the allowable content of those files. This has been available for some time now so we have seen firms undertaking projects to get their data in the right format for reporting. Again this depends slightly on the reporting phase that the firm has to adhere too, for firms who do not have an obligation to report until phase four there is an extended period to allow for readiness. I think firms are very aware of their obligations and we have seen firms undertaking testing already. We have had a solution available since June 2018 to assist firms in their data readiness phase, which we have seen firms utilise to ensure that their data gets more compliant to the latest standards.

On 31 October, ESMA published the XML final schemas. I think firms will need to analyse the new documents and begin the implementation process of those messages.

Could the December release of the level three text cause a delay given that firms will only have from December to April to prepare?

The timelines for reporting for SFTR are in the official journal publications. The March official journal publication contained information relating to the field content, firms have been working with that information so it would surprise me if there was a delay given the information that has been available for some time now.

What are the main sorts of questions and concerns you receive from clients regarding SFTR? Is there a pattern to these questions?

The type of questions that we receive are very varied because there are different implementation timelines. We get some questions from the buyside relating to specific trading models, for instance firms in phase three who do not need to report in April but need to provide the sell side who have a reporting obligation in phase one with specific allocations to block trades. Some of the buyside firms are therefore having to think about how they provide that data, the actual allocation data on the beneficial owners in the report up to the sell side ahead of their reporting. MTS has, for example, seen an increase in electronic trading on its dealer-to-client BondVision Repo platform, where the ability to seamlessly share allocation information between the buyside and their dealers is a key element of the STP on offer.

Another question that we receive quite a lot is around the regulatory timeline, as CCPs are mandated from phase two and not phase one. The question of how firms going to get their data and their unique trade identifiers (UTI) ready and reported when the CCP doesn't become reportable until later continues to come up. Working closely with LCH, we know that they are actually going to be reporting early and the UTI generation algorithm has been published on their website. LCH are offering an enhanced suite of reports to its members to assist them in their reporting obligations as well as working with ourselves to offer the assisted reporting solution. Where we find specific challenges in the market are working hard to make sure we have solutions to help the industry.

A recent survey has highlighted that firms are holding out on picking their TRs for SFTR because the TRs are not publishing their pricing. Have you published your pricing? What have you heard about other TRs?

SFTR is quite unique in the fact that we have seen people hold off selecting their TRs but the main reason seems to be because they are selecting vendors first. Because of market fragmentation, a lot of firms might have a number of different systems that they are using to trade in different ways depending on the products.

For securities lending, they might be using agents or for repo trades they might be executing more bilaterally or use central clearing. There are also different places that data might be located and a number of different systems the data might be reported from. We are seeing the market coming together to use innovative solutions such as the MTS SFTR blotter, the LCH assisted reporting module, or even other vendors to allow the various reports to be maintained more centrally. There is also an array of offerings that have additional services such as pre-matching and UTI generation. The vendors would then report to the TRs and we do have active vendor relationships. We have over 50 different partners across our UnaVista offerings. **SLT**

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Time is running out

David Lewis of FIS surveys the state-of-play for the industry in the final run up to SFTR and addresses the many hurdles yet to be cleared

If there were a list of phrases rarely heard, "that regulation came around quickly" is, I would venture, quite near the top, probably somewhere near "Brexit is easy, isn't it".

However, here we are, around five months away from the potentially seismic impact of Securities Financing Transactions Regulation (SFTR). It seems like something that has been in the far distance for so long is suddenly around the corner. And it appears not everyone is on schedule, including the regulator itself.

A survey by the regulatory reporting provider, Cappitech, covered recently in Securities Lending Times, announced that two-thirds of firms will not be fully ready for SFTR go-live. The survey covered a wide range of firms, from banks and asset managers to trade repositories and non-financial entities, but that does not detract from the worrying headline. SFTR can in no way be described as news to any direct or indirect participant in the securities finance industry, whether inside the jurisdiction of European Securities and Markets Authority (ESMA) and the EU, or outside of it. However, according to the Cappitech survey, 11.5 percent have not started planning yet. Of course, if that contingent is made up of the non-financial entities that took part in the survey, then it could be understood. If that is not the case, some organisations are certainly appearing to be leaving this to the last minute.

It has also been a long road to get to this point. FIS has put significant resources into the analysis, design and development of our SFTR solutions, but that project, along with the work of every other provider and market participant, has been at the mercy of the regulator's timetable. Taking the logical approach of matching work plans with the roll out of the regulation itself, we are all looking to the actual reporting outputs. Most will have already worked through all the sourcing, storing and management of new data elements to the re-engineering of booking and trade management processes, leaving report generation to the end, in line with the release of the XML schemas from ESMA. Now, it appears the schemas are not only being issued behind schedule, but they continue to include errors.

The timetable for issuance of the schemas was always going to be tight, particularly when accounting for the major project milestones to be considered in the run-up to go-live, such as connectivity to your chosen trade repository, testing and, of course, a healthy dose of contingency. Factor-in the impending Christmas break in the middle of the remaining timeframe with the associated year-end freezes, and suddenly the headline shouting that two-thirds of firms potentially not being ready starts to look not only believable, but perhaps even a little low!

The roll out of the predecessors of SFTR, namely the European Market Infrastructure Regulation and the Markets in Financial Instruments Directive, were beset with issues at go-live, not least due to the sheer quantity of participants seeking to complete their projects in the weeks, or even days, before the regulatory go-live date.

A contact at one trade repository recounts the story of a major firm contacting them on the last Friday before go-live, demanding 5,000 new accounts be set up for the Monday. While the example may not translate perfectly to the implementation of SFTR, the risk of not allowing every stakeholder in your process time to get up-to-speed is clearly illustrated. According to the survey, 7 percent of firms are planning to do just that – rush the testing stage through in the last month before go-live. Perhaps more alarmingly, 11 percent indicated that they were not planning to test at all. Again, as above, if these are the non-financial firms in the survey, who have outsourced their reporting to their counterparts, then perhaps that is less of a concern, if they are paying proper attention to their oversight responsibilities, of course.

For the remaining companies, it may well be admirable for your firm to be ready, but what about your market counterparts, and those providing services to you? Those leaving testing so late will put providers and their counterparts under serious and unwelcome pressure. One service provider has recently issued a sign-up deadline, which is understandable. At FIS we have been assisting our own clients through the necessary upgrades and changes required; this is not a do-it-yourself exercise for any stakeholder.

Business process re-engineering is a potentially substantial segment of the SFTR readiness project for any market participant. Considering the relationship between market participants, their counterparts and providers, much is potentially going to have to change, and unless that is already well under way, it may already be too late.

To learn from the Cappitech survey that only 28 percent of firms had started implementing their solution would suggest that this part of the project may well be building-up significant go-live risk. Have all the market participants within the jurisdiction of ESMA compared their booking, re-rating and return processes to ensure their trades have a good chance of matching at the trade repository? Have those same participants agreed at a counterparty specific level who is going to produce and who will receive the unique trade identifier (UTI)?

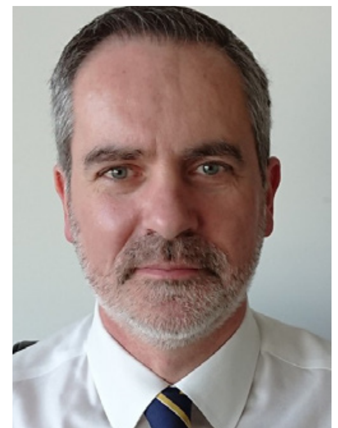
Given all that could go wrong with the roll out of SFTR, and arguably already has in terms of the issues with the original reporting specifications, their multiple revisions, the unanswered queries and now the reporting XML schemas, it is perhaps most surprising that 9 percent of the respondents to this survey claimed to be “fully ready”.

With so many potential gaps and issues, this number appears to be very high, excluding the chance that they are outsourcing their reporting and have nothing more to do. Either that, or they have totally misunderstood the gravity of SFTR and its requirements.

Many column inches have been spent on the genesis, roll-out and now impending implementation of SFTR. As an industry, we have had ample time to prepare for the launch of what will be the most detailed reporting requirements to affect our business ever. As a result, it would not be unreasonable to assume that the regulator could justifiably take a dim view of market participants who are not ready to comply through a simple lack of effort or organisation.

However, it is also true to say that there have been more than a few bumps in the road as the industry has moved toward implementation, providing some justification for issues that may arise next April. Given some of the worrying statistics in the Cappitech survey, it appears that it is not a question of whether there will be issues, but how bad they will be for those that are not sufficiently prepared.

David Lewis
Senior director
securities finance
FIS



Comings and goings at ISLA, IHS Markit, DeltaOne and more

IHS Markit has bolstered its securities finance team with the hire of Lou Carvajal, based in New York.

Carvajal has joined the data provider as a director in its securities finance business. He will report to Melissa Gow, executive director, securities finance.

At IHS Markit, Carvajal serves as a senior product specialist, providing global product and industry expertise to the firm's largest sell- and buy-side customers.

A spokesperson for IHS Markit said that Carvajal's knowledge of data, analytics and best practices will help drive its securities finance product roadmap and ensure customer satisfaction.

Carvajal was previously vice president of securities lending, international and domestic, at ABN AMRO Securities from 2010 to 2018.

Before then, he worked at Fortis Securities between 2004 and 2010. He initially served in international stock loan operations and later became an associate vice president for securities lending trader.

Between 2000 and 2004, Carvajal was a securities lending operations manager at Barclays Capital.

The International Securities Lending Association (ISLA) has welcomed nine newcomers to its 15-strong board, as well as confirming the return of its current chair and deputy chair for a three-year term.

ISLA's newcomers include: Poya Agha-Bozorgi of Morgan Stanley; Harpreet Bains of JPMorgan Chase; Ina Budh-Raja of BNY Mellon; Matthew Chessum of Aberdeen Asset Management.

Also joining for the first time are Arnaud Fransioli of Société Générale; Matt Glennon of Citibank; Tanja Hauenstein of Credit Suisse; Mat McDermott of Goldman Sachs; and Ed Oliver of eSecLending.

Jonathan Lombardo from Deutsche Boerse will remain as chair, while Alessandro Cozzani from Bank of America Merrill Lynch retains his deputy chair position, and Paul Bradford from ING will continue to be the ISLA's treasurer.

Meanwhile, Stefan Kaiser of BlackRock, Eicke Reneerkens from Union Investment, and Ueli von Burg, of Zürcher Kantonalbank will be returning to the board.

In total, the 15 members represent multiple global and regional firms as well as functions across the industry.

According to Lombardo the new board is "by far the most diverse ISLA has experienced".

Jonathan Addy has left his role at DeltaOne, part of IHS Markit, to become a senior technical architect for exchange-traded funds (ETF) data services at ULTUMUS.

ULTUMUS is a global provider of data creation, management and distribution services for index benchmark and exchange traded products. It is focused on the index and ETF data space and sees opportunity where existing vendors have not updated their platforms and products.

Addy, who is based in London, will work on the representation of ETF data in the ULTUMUS user interfaces and application programme interface.

Commenting on his new role, Addy said: "I have always been impressed with ULTUMUS and the growing team, so when the opportunity to join them came up, I didn't hesitate."

"I look forward to working alongside some of the industry's most experienced professionals that have created a highly customisable and agile platform built on the most modern data architecture."

Bernie Thurston, CEO of ULTUMUS, commented: "With Jonathan Addy having now joined us we have achieved our strategic goal of bringing together the most experienced and talented people across this fast moving and exciting sector."

Thurston added: "Where once people wanted to be within the largest of firms, now the attraction is to smaller, nimble and more innovative firms that can drive change in the sector and are free from legacy dependencies."

Previously, Addy spent five years as a senior technical architect at DeltaOne where he oversaw the web-enabled release of the complete DeltaOne Solutions product set.

He first joined IHS Markit as a vice president in 2007 before joining DeltaOne in 2015.