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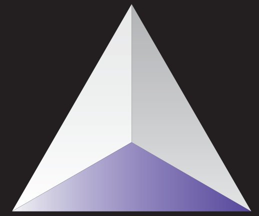

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ECB allows PSPP securities

The European Central Bank (ECB) has made the holdings of securities purchased under the public sector purchase programme (PSPP) available for securities lending.

The implementation of this activity has been delegated to its existing lending agent Deutsche Bank under the terms and conditions determined by the ECB.

The ECB has stated that it may revise these terms and conditions.

Holdings purchased by the ECB under the Securities Markets Programme that are also eligible under the PSPP will be available for lending at the same conditions.

The ECB's securities lending arrangements are designed to allow eligible counterparties, any time, to borrow securities at a fixed fee of 40 basis points. This fee is the difference between the repo and reverse repo rates.

The term is a fixed maturity of one week, and the ECB has offered the possibility of rolling over the transaction on a week-by-week basis for up to three times with the fee increasing by 10 basis points at each time.

According to the ECB, the arrangements are aimed at primary dealers of euro area sovereign bonds and at other institutions with "market making commitments", provided that they fulfill all the legal requirements for the given securities lending activities.

This involves, in particular, the signing of what the ECB has deemed the "relevant contractual documentation" with the securities lending agent, Deutsche Bank, subject to the approval by the ECB.

The Bank of Italy has made securities purchased under the PSPP available for lending, as of 11 May, under the governance of Clearstream Banking.

The securities lending service will include fail coverage activities in support of settlement (Automated Securities Lending and Borrowing Service, or ASL) and strategic market activities (Automated Securities Lending Plus, or ASLplus).

Lending of PSPP securities holdings is to take place on a cash neutral basis. This means that repo transactions against cash collateral will be accompanied by a fully offsetting reverse repo transaction for the same value date and, in principle, with the same counterparty.

A fixed spread fee of 10 basis points will be applied to ASLplus transactions, which is considerably cheaper that the European Central Bank's current fee of 40 basis points.

The securities lending programme itself is governed by Clearstream Banking's standard terms and conditions.

The Bank of Italy said that it may revise these parameters if necessary and will inform the markets via its website.

Alternative investment funds at risk from asset segregation

Asset segregation as proposed under the Alternative Investment Fund Managers Directive (AIFMD) will compromise triparty collateral management and securities lending, according to Ross Whitehill, managing director of BNY Mellon's markets group.

A recent European Securities and Markets Authority (ESMA) consultation paper proposed the enforced segregation of alternative investment fund assets across all levels of the custody chain. This could affect the ability of funds to utilise triparty collateral management services, and to participate effectively in securities lending.

The change also has the potential to affect UCITS funds, depending on regulatory harmonisation with AIFMD.

SLTINBRIEF

Cash collateral
This form of indemnification may be about to lose its crown

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CIBC Mellon and CASLA's Rob Ferguson outlines why business in Canada is booming

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The ECB has had to make unexpected corrections to the course of its QE programme

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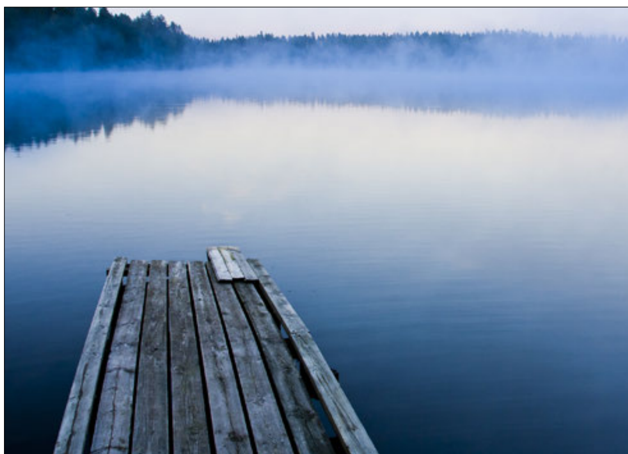

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Whitehill said: "The impact on funding and liquidity in the market will, we believe, be very significant affecting growth and investment in Europe."

The proposed asset segregation rules are intended to protect the interests of investors by preventing assets from being exposed to negative events, such as bankruptcy of a third party.

Whitehill argues, however, that taking this too far by segregating assets down to sub-custodian level could in fact increase, rather than mitigate, counterparty, operational and systemic risk.

"The proposed segregation approach actually increases investor risk along the post trade chain," he said.

"It also increases systemic risk. This is due to the substantial increase in accounts, a corresponding increase in movements of securities, and in particular the inability of alternative investment funds to function in a triparty environment."

"There will also be increased settlement and operations risk because market deliveries will be necessary, rather than intra—day book entry books and records management."

He also suggested there would be an impact on pension funds, insurance companies and other non-alternative investment fund counterparties, as there will be no third-party collateral managers available to support related transactions such as repo and securities lending.

Whitehill said: "Collateral management is a highly specialist function and—given the demand for, and likely scarcity of eligible collateral—it is highly unlikely that funds will be in a position to effectively support their collateral management requirements themselves."

"The removal of triparty collateral management will place an inordinate burden on the funds themselves and their counterparties, forcing them into bilateral collateral management."

Collateral optimisation key to outsourcing decisions

Collateral optimisation should be taken in to account when considering outsourcing, according to a report by Sapient Global Markets.

As various regulations start to take effect, buy-side firms are increasingly evaluating the benefits and costs of in-house solutions, compared to outsourcing.

The report suggested that collateral will soon be treated as a new asset class, and so, in addition to satisfying counterparty needs and regulatory requirements, firms will also have to generate revenue through collateral trading, optimisation of assets and re-use of collateral.

In order to keep costs low, it will be important to optimise collateral allocation, through trading and transfer, while also taking in to account haircuts, eligibility and alternatives.

This added complexity, however, could mean that managing collateral in-house is easier and more efficient, however, the added complication and overlapping nature of regulations increases the risk of rising costs, and so outsourcing can be used to ensure that costs remain predictable.

The report identified three key areas that firms should consider when deciding whether to use in-house or outsourced services: whether they have the qualified personnel in-house, or if they would have to invest in training and hiring; whether they can standardise daily operational tasks to minimise the risk of failures; and whether frequent changes could lead to more uncertainty.

It concluded that, while benefits from collateral optimisation and transfer can have a positive effect on cost structures, it could also decrease the costs of outsourcing.

Solutions will depend on the structure of a firm and the fee structure of third-party providers, but either way, according to Sapient Global Markets, collateral optimisation should be a significant factor in the decision-making process.

BNY Mellon drastically reduces intra-day credit

BNY Mellon has completed its triparty repo risk reduction initiative in support of the recommendations of the Task Force for Tri-Party Repo Infrastructure Reform.

As part of these efforts, BNY Mellon reduced the secured credit extended in the triparty repo market by $1.44 trillion, or 97 percent, resulting in the practical elimination of such credit in its programme, which was a critical goal the task force outlined in 2012.

This milestone marks the conclusion of a multi-year cooperative effort by BNY Mellon, its clients and other market participants to restructure the US triparty repo market.

In addition to the intra-day credit reduction, BNY Mellon introduced a wide range of enhancements including Automated Deal Matching, which captures instructions independently from repo counterparties and ensures all parameters of a triparty repo trade match prior to settlement.

This enhancement intends to improve the timing, transparency and accuracy of such trades.

Elsewhere, Auto Collateral Exchange will allow triparty repo trade collateral to automatically substitute securities for cash, significantly upgrading the way collateral is optimised and allocated.

Other enhancements such as rolled trade functionality, rebalancing capabilities and a new settlement algorithm have also been introduced.

"As the market leader for triparty collateral management, we embraced the task force recommendations and proactively addressed the necessary changes without disrupting the market," said Brian Ruane, CEO of broker-dealer and triparty services at BNY Mellon.

"Through a comprehensive set of operational and technology improvements, as well as the strong partnership with our clients and other market participants, we have significantly

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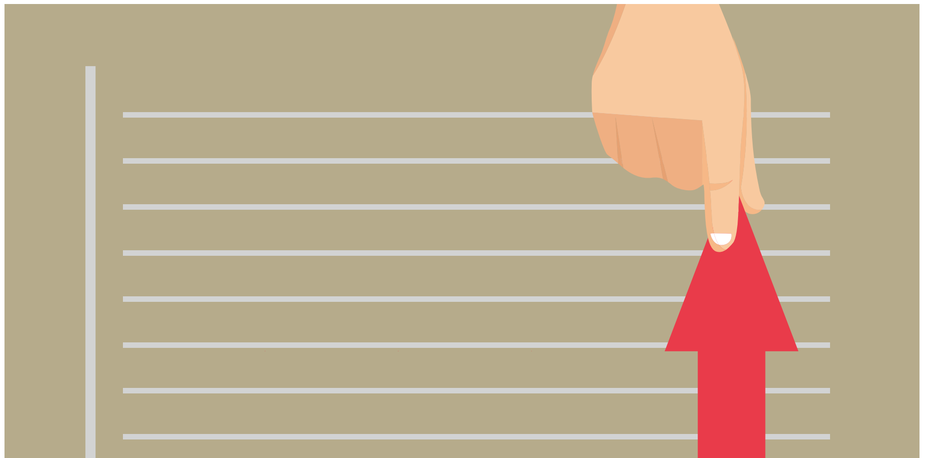
reduced systemic risk and positioned our clients for success moving forward in this market."

BNY Mellon said its strategic focus on aligning its technology and business teams to develop innovative solutions to complex problems helped drive the transformation of the company's triparty repo offerings.

Kevin Fedigan, chief information officer of broker-dealer services at BNY Mellon, added: "In addition to properly aligning our technology and business resources, keys to the programme's success included the systematic phasing in of incremental solutions, creating close partnerships with clients and industry participants in defining and confirming requirements, communicating actively with all stakeholders throughout the process, and delivering value-added capabilities that drove adoption."



Decline in cleared contract volume for OCC

OCC's cleared contract volume decreased 8 percent in April compared to the same month in 2014.

Average daily volume also dropped 9 percent in 2015.

In April 2015, securities lending central counterparty activity increased by 16 percent in new loans from April 2014 with 112,978 transactions during the month.

OCC's stock loan programme reported "strong" volume numbers in April with year-to-date activity up 12 percent.

Year-to-date stock loan activity increased by 12 percent from 2014 with 430,442 new loan transactions in 2015. The average daily loan value cleared by OCC in April was $186.5 billion.

Positive April for OneChicago

OneChicago saw an increase of 2 percent year-over-year in April 2015 despite a decrease in year-to-date volume of 11 percent compared to April last year.

Open interest increased 20 percent year-over-year to 626,984 contracts on the equity finance exchange at close-of-market.

In the latest figures, 564,379 blocks and EFPs were traded on OCXdelta1.

At month-end, 57 percent of the open interest was in OCX.NoDivRisk products, an equity finance tool that removes dividend risk for customers carrying synthetic equity delta exposure.

GIC adopts Omego Alert

Singapore's sovereign wealth fund GIC Private Limited has adopted Omgeo Alert, a web-based global database for the maintenance and communication of account and standing settlement instructions (SSIs).

The fund stated that it adopted the solution in order to deliver further improvements in post-trade operational efficiency.

GIC has said that it wanted to enhance its enterprise trade lifecycle platform as part of a two-stage process.

Phase one involved the importing of SSIs into Alert, with a focus on fixed income instructions, in Q3 2014.

GIC is now embarking on the second phase of that project: loading SSIs for equity trades into Alert. This is scheduled to go live in Q2 2015.

GIC first engaged Omgeo, a wholly owned subsidiary of the Depository Trust & Clearing Corporation (DTCC), in 2007 when it adopted Omgeo Central Trade Manager (CTM) for the automated central matching of domestic and cross-border equities and fixed income trades.

Additional asset classes, including repos, exchange traded derivatives and synthetic equity swaps, are also available to other clients when they use Omgeo CTM.

"GIC's adoption of Alert is symbolic of a broader trend among companies in Asia Pacific to improve the management and communication of SSIs with global counterparties," said Nellie Dagdag, executive director of DTCC Asia.

"With Alert, market participants are able to increase operational efficiencies since the solution automatically enriches trades in Omgeo CTM with accurate and compliant settlement and account instructions."

Compliance with growing regulation, reputational risk from failed trades, and lower operating costs by removing manual processes are the key reasons companies in Asia

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Pacific are increasingly automating their trade confirmation processes, according to a recent study commissioned by Omgeo.

Bumper April for Clearstream

The monthly average outstanding for Clearstream's global securities financing (GSF) services reached €628.4 billion in April 2015.

The combined services, which include triparty repo, securities lending and collateral management, collectively experienced an increase of 7 percent over the April 2014 total of €589.8 billion.

The GSF monthly average outstanding has grown 8 percent since the same date in April 2014, when it stood at €582.5 billion.

Also in April 2015, the overall value of assets under custody held on behalf of Clearstream customers registered an increase of 10 percent to €13.3 trillion, compared to €12.1 trillion in April 2014.

Securities held under custody in Clearstream's international business as international central securities depository (ICSD) rose by 11 percent from €6.4 trillion in April 2014 to €7.1 trillion in April of this year.

Those securities held under custody in the German CSD increased 10 percent from €5.7 trillion in April 2014 to €6.3 trillion in April 2015.

For the period year-to-date April 2015, the combined value of assets under custody in the German domestic CSD and global ICSD business increased 10 percent compared to the same period in 2014.

Elsewhere, 3.8 million ICSD settlement transactions were processed, a 6 percent increase over the April 2014 total of 3.6 million. Of all international transactions, 82 percent were over-the-counter transactions and 18 percent were registered as stock exchange transactions.

On the German domestic market, CSD settlement transactions in April 2015 reached 7.7 million, 18 percent more than in April 2014. Of these, 64 percent were stock exchange transactions and 36 were done over-the-counter.

For the period year-to-date April 2015, the number of settlement transactions processed for the German domestic CSD and global ICSD business combined increased by 13 percent compared to the same period in 2014.

Mathias Papenfuß, head of operations and member of the Clearstream board, commented: "Target2-Securities is just around the corner and the industry is in a very complex transition phase. In addition, regulatory challenges increase the pressure on customers and bind their resources."

"Clearstream is a very reliable partner with a comprehensive portfolio of services designed to relieve this burden and our April figures are further proof that our customers appreciate this offering."

"The next few months will be transformational for the industry and we look forward to supporting our customers going forward."

OneChicago gives its two cents

OneChicago has requested guidance from the Internal Revenue Service (IRS) and US Department of the Treasury concerning three issues related to Section 1058 of the Internal Revenue Code.

The request has arisen in response to the IRS and US Treasury's invitation for public comment on recommendations for items that should be included on the 2015-2016 Guidance Priority List.

OneChicago has requested guidance on whether a taxpayer who uses an exchange-traded and centrally-cleared derivative, rather than a bilateral, over-the-counter (OTC)

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derivative, to provide for the return of securities under section 1058 would be eligible for the non-recognition treatment afforded by that section.

Guidance has also been requested regarding whether Section 1058 imposes a requirement on all those that transfer securities—organisations and individuals—to be able to reacquire the transferred securities within five days.

Finally, OneChicago has asked for guidance on whether a taxpayer who has transferred securities to a transferee in accordance with the requirements of Section 1058 and subsequently executes a hedging transaction with a third party would remain eligible for non-recognition treatment of the initial transfer under section 1058.

OneChicago commented: “The lack of clarity regarding these three issues has caused market participants to defer moving certain bilateral derivatives activity onto regulated exchanges.”

SunGard’s hottest stocks

Much of the UK securities lending market has seen buoyancy following a surprise majority win for the Conservative party, according to SunGard’s Astec Analytics.

This has reassured investors and benefited companies such as Premier Oil (PMO.L), as many analysts have suggested the win would offer benefits for those companies operating in the North Sea.

As its share price gained ground, short sellers began to cover their positions, with borrowing volumes falling about 11 percent.

Transocean’s (RIG) share price has also gained ground despite mixed numbers.

On the borrowing front, these gains have seemingly triggered a bout of short covering, with volumes falling 9 percent in just one day.

In the Americas, Time Warner Cable (TWC) has seen fresh attention as news emerged that Charter Communications was arranging a debt package in order to pursue its merger with the cable giant.

Astec commented: “As its shares lost ground, so too did borrowing volumes however, hinting at an increase in short covering—the number of TWC shares being borrowed falling 30 percent in the week.”

In contrast to oil company activity in the UK, US renewable energy producer Clean Energy Fuel Corporation (CLNE) has caught focus after UPS said they would be using renewable natural gas for part of its delivery fleet—Clean Energy producing the first such gas available in commercial quantities. Despite this, its share price did see some pressure as a number of investors took profit on the back of recent highs, while on the borrowing front Astec’s data suggested demand to short sell picked up—the cost of borrowing climbing from under 40 percent to a peak of more than 65 percent.

Japanese tech giant Sharp (6753) has secured the top position in Astec’s list for the Asia Pacific region after it said its upcoming restructuring plan could include an accounting adjustment that would effectively wipe out much of the underlying value of current shareholder investments—bringing about a 30 percent decline in the stock.

On the borrowing front, Astec’s data has suggested short sellers have been covering positions for more than a month, with volumes now down 12 percent compared to 1 April.

Mixi (2121) has also seen interest ahead of its latest earnings numbers; investors seemingly taking on positive expectations as the share price has climbed.

Astec’s data has also suggested short sellers have been increasing their stakes, with volumes up 20 percent over the past six weeks.

ESMA approves Asia Pacific and China clearinghouses

ESMA has recognised ten third-party central counter parties (CCPs) in the Asia Pacific and

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China region, allowing them to provide clearing services to members or venues in the EU.

The approvals are in jurisdictions that have been assessed as equivalent by the European Commission with regards to their legal and supervisory arrangements for CCPs.

The decision follows several other steps, including the conclusion of cooperation agreements with the relevant authorities and consultations with other authorities and central banks.

Australia's ASX Clear (Futures) and ASX Clear Pty Limited have been newly approved, while Japan Securities Clearing Corporation and Tokyo Financial Exchange from Japan have received approval. Hong Kong Securities Clearing Company Limited, HKFE Clearing Corporation Limited, OTC Clearing Hong Kong Limited and The SEHK Options Clearing House Limited all made the cut.

Finally, in Singapore, Central Depository (Pte) Limited and Singapore Exchange Derivatives Clearing both received CCP approval.

Macro managers build resiliant short positions

Global macro managers that have built up short positions on European rates proved to be resilient in April, according to a brief from Lyxor.

Some macro managers were up 2 percent while others, which were most exposed to European equities, were down 1 percent.

In the commodity trading advisor (CTA) space, Lyxor's data showed that losses were broad-based and reached high single digits in some cases.

Philippe Ferreira, head of research for Lyxor's managed account platform, commented: "The bond market selloff that took place in Europe appears to be the result of several factors: rich valuations, a rebound in energy prices lifting inflation expectations and improved growth conditions in the region."

According to Ferreira, the extent of the price action is technical and partly related to the fact that in "thinly traded" markets due to the European Central Bank quantitative easing, macro managers have been increasing their short positioning on European rates.

He continued: "Several prominent fixed income managers have been vocal on the opportunity to short the bund a few weeks ago, and, from what we can see in the industry, have actually implemented these views within their portfolios."

Mixed results for SS&C

The gross return of SS&C GlobeOp's Hedge Fund Performance Index for April 2015 measured 0.34 percent, down from 1.30 percent in the previous month.

On a more positive note, hedge fund flows as measured by the SS&C GlobeOp Capital Movement Index advanced 0.92 percent in May, up from a 1.14 percent decline in April.

"May 2015 saw the largest increase in the Capital Movement Index in the past 12 months, as inflows easily outpaced outflows. In fact, outflows were the lowest recorded since the index's inception in 2006," said Bill Stone, chairman and CEO of SS&C Technologies.

The Capital Movement Index represents the monthly net of hedge fund subscriptions and redemptions administered by SS&C GlobeOp.

This monthly net is divided by the total assets under administration for fund administration clients on the SS&C GlobeOp platform.

The Capital Movement Index has declined 2.24 points over the past 12 months, with the next publication date set at 11 June 2015.

SS&C GlobeOp's data represents approximately 10 percent of the hedge fund industry.

A focus on regulation

BCBS239: removing manual work-arounds

An overreliance on manual work-arounds and tactical mitigants are preventing globally systemically important banks (G-SIBs) from realising the full benefits of BCBS239.

In its second progress report published in January 2015, the Basel Committee on Banking Supervision revealed that almost half of G-SIBs questioned did not believe they would comply with all 11 banking principles set by the regulation before the deadline of 1 January 2016.

Attempts to establish strong data governance, aggregation, and architecture processes necessary for compliance have proved difficult to achieve for many of the G-SIBs. To address this challenge, firms are implementing large-scale projects to improve their IT architecture and infrastructures. but many are also relying heavily on manual work-arounds and tactical mitigants in their efforts to achieve compliance.

Manual work-arounds and tactical mitigants are typically major constraints on the flexibility, adaptability and operational robustness of BCBS239 solutions. They may achieve compliance on a superficial 'box ticking' level, but they do not go to the heart of addressing many of the deep seated challenges surrounding risk data aggregation and reporting that BCBS239 was introduced to address.

There are of course occasions when manual work-arounds and tactical mitigants (such as end-user applications) are sometimes difficult to avoid. However, it must be remembered that they usually increase the 'process debt', which normally creates a heavy penalty to be paid at some point in the future.

As with any debt that accumulates over time with a crippling rate of interest, technical and process debt can reach unmanageable proportions as complexity rises unabated. This situation increases the potential risk to a firm and also inflates the cost to eventually make a more strategic change in future.

Banks need to understand and monitor the amount of debt they are storing up for the future, and ensure that there are plans and a budget in place to address this challenge. One such plan would be to include implementation debt assessment and remediation strategies into regular technical and business audits.

Few people deny that tackling BCBS239 is a daunting challenge for firms, but many must be mindful of the consequences of relying too heavily on manual work-arounds and tactical mitigants. They can bring short-term gains, but they also compromise the long-term value and benefits.

Firms should now be identifying how they can make the transition towards implementing more strategic solutions, which give them the best chance of meeting the imminent compliance deadline, and reduce any long-term technical and process debt.

Alan Morley
Anti-money laundering and risk practice lead (US)

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The king is dead, or is he?

Is the ruling monarch of indemnification about to lose its crown? David Lewis of SunGard's Astec Analytics takes a look

The financing industry is not alone in its view that 'cash is king'—cash is the lifeblood of almost all business and, like blood, is something you cannot do without. But is the king under threat? Is its popularity on the wane? It could certainly be argued that cash is no longer as popular as it once was in the real economy—and by cash we mean physical notes and coin. With the advent of the mobile wallet and contactless cards, more and more transactions are being undertaken electronically, passing digital zeroes and ones across the internet for your latte rather than a pile of metal coins, or in most cases, more like a roll of notes.

In our industry, it has been suggested that cash is also in decline, at least as a form of collateral. There are potentially a whole host of reasons for this, and reasons why it is not true, or expected to happen. For the move away from cash camp, we have the perception of risk for one. Looking back at the financial crisis from 2007, the financing industry, and in particular securities lending, was hit particularly hard. Losses were accrued, but in the vast majority of cases these were limited to the cash reinvestment programmes associated with the cash collateral taken by the lenders.

This analysis doesn't seek to analyse what actually went wrong in that scenario, just to observe that it occurred and certain behaviours have changed as a consequence. Few can argue that the end result of this has been much tighter reinvestment controls and credit criteria, and even fewer could argue that this is a bad thing from a risk management point of view, or that it has curtailed the additional revenues or reinvestment premium that clients could earn from these investments.

The drop in reinvestment premium is potentially, in itself, part of the reason why some market participants are moving away from cash as collateral, because without the premium available, the incentive to take cash is reduced. As with many economic issues, however, there is always the other hand to count on. Fighting in the cash corner is the need for liquidity—the motivation to lend securities is not always just to earn incremental revenues of course, it is often to raise cash for liquidity or other financing purposes. New regulatory pressures have also played their part here. The need for liquidity has driven market demand for high quality liquid assets (HQLAs) and this is expected to continue as the regulations take hold. What is that data telling us, though? Is the mix of cash and non-cash collateral usage changing and does that change differ across the regions?

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ISLA is delighted to announce its two keynote speakers for this year's **24th Annual Securities Finance and Collateral Management Conference**. The opening keynote speech will be given by **Cristina Casalinho**, Chairman & CEO at the Portuguese Treasury and Debt Management Agency and the conference will conclude with a speech by **Sir Clive Woodward OBE**, Former England Rugby Coach and Winner of the 2003 World Cup.

SPECIAL KEYNOTE ADDRESSES

Cristina Casalinho

Chairman & CEO

Portuguese Treasury and Debt Management Agency

Sir Clive Woodward OBE

Former England Rugby Coach and Winner of the 2003 World Cup

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FULL AGENDA LIVE

Moderators and speakers have now been announced! For all the latest agenda developments join our linkedin group.

Figure 1 shows the indexed value of fixed income assets lent against non-cash collateral from July 2012 to May 2015. Note that the values for Asia are logged against the right hand axis to allow for their scale compared with Europe and North America. Asia has seen a dramatic upswing in the value of fixed income assets in our sample, which are lent against non-cash collateral. Europe has also exhibited a significant increase in the value on loan against non-cash collateral, although more than doubling over this period it is a small increase compared with the meteoric rise in Asia.

It should be noted that there are two additional factors to be considered when looking at these numbers: SunGard's Astec Analytics sample data continues to grow as we expand our offerings and coverage globally, particularly in Asia and Europe, as well as the general rise in asset values, especially quality government debt, which is a significant part of the data under analysis here. Even taking these outside variable influences into account, both regions have shown significant change over the last three years. The rise in value for US fixed income assets has been less dramatic, more like a 10 percent shift, but in what is likely to be the largest market by value in the world, 10 percent is not insignificant.

The rise in value on loan against non-cash collateral is one aspect of interest, but the proportion of those assets lent against cash and those against non-cash collateral is also of interest for a number of reasons. Figure 2 shows the proportion of fixed income assets by value lent against non-cash collateral for the European, North American and the sum of the global markets. Note that the plot lines shown represent the proportion of value lent against non-cash. As this figure rises, so the opposing value lent against cash falls. The cash collateral plots have been omitted from Figure 2 to aid clarity.

The European market, which is traditionally a non-cash collateral dominated environment, is shown on the graph to be increasingly non-cash orientated. In the middle of 2012, the data indicates that the European fixed income market was lent against non-cash between 60 to 65 percent by value. By Q1 2015, this proportion is in the 80 percent range. North America has also risen, although by less in absolute terms. Commencing in the mid-40s, the proportion of fixed income lent against non-cash collateral actually fell through 2013 and 2014, hitting a low point of around 40 percent a year ago. Since that time, the rise has been slow but steady, posting a score just above 50 percent in April and May 2015.

As noted above, not a stellar change on the face of it, but a 5 to 10 percent change in a market with outstanding balances measured in hundreds of billions is a change that has many ramifications that need to be addressed.

Historically, a market dominated by cash collateral, changing to have more than half of assets being lent against non-cash collateral, will affect pricing and the rates charged for assets, as well as risk management profiles as collateral management has to adapt, meaning trading systems may need to be upgraded or changed to manage an increasing proportion of collateral types rather than just the US dollar.

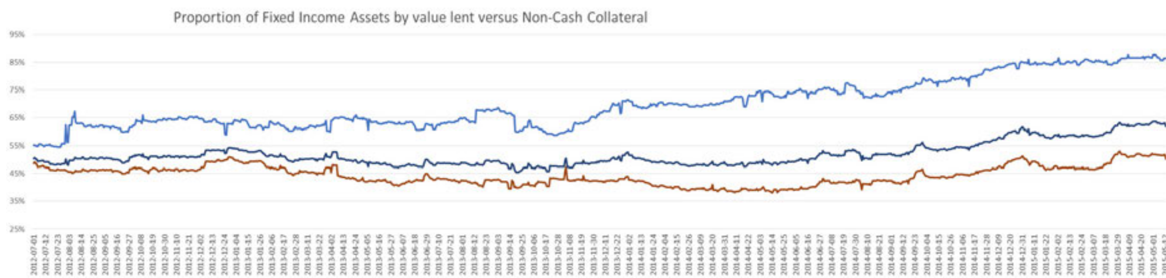
As markets change their perspectives on the type and make up of collateral they take, they will need to adapt systems and processes as well as develop new knowledge and gather experience in managing the new regime. With many pieces of new legislation yet to actually bite, it is quite likely that the proportion of non-cash collateral traded will continue to rise. It may be too premature to say that the king is indeed dead, but it seems the sun may be beginning to set on this particular monarch's reign. **SLT**

David Lewis
Senior vice president
SunGard's Astec Analytics

Figure 1: Indexed values on loan against non-cash collateral

Source: SunGard's Astec Analytics

Figure 2: Proportion of fixed income assets lent against non-cash collateral



Source: SunGard's Astec Analytics

The case for Canada

Rob Ferguson, senior vice president of capital markets and product delivery at CIBC Mellon and president of the Canadian Securities Lending Association, outlines why business in Canada is booming

Canada's securities lending market is among the world's largest and most active, reflecting widespread confidence among participants for their counterparties, agent lenders and other stakeholders. Canada currently accounts for approximately 10 percent of the global securities lending market, making it the industry's second market overall (behind only the US, and ahead of Germany, France and Japan).

Central to this confidence is Canadian participants' continuing focus on due diligence, their consistent risk management track record, and technological innovation—helping to meet the needs of borrowers and beneficial owners, even as their needs evolve.

Demand for Canadian assets has continued to grow, thanks to strong credit ratings as well as very healthy demand for Canadian bonds—in particular from foreign sovereign wealth funds and central banks following the establishment of the Canadian dollar as an official International Monetary Fund reserve currency in 2013.

Canada's triple-A rating and risk-management acumen only tell part of the story, of course. At around 43 basis points on average, Canada also boasts some of the most affordable equity borrowing rates in the business, more than 50 percent lower than European trading fees and nearly one-third the cost of the Asia Pacific region, according to recent research from DataLend.

Despite a historical emphasis on non-cash collateral with a fixed income focus, in recent times Canadian regulators have worked collaboratively with industry players to expand the parameters of qualifying lendable securities. Two years ago, the Canadian government approved an amendment to Section 260 of Canada's Income Tax Act, allowing the likes of exchange-traded funds and real estate investment trusts to participate in securities lending.

In Canada as in many other regions, a flexible lending structure is a key contributor to lending success. Owners willing to incorporate greater flexibility—particularly around collateral acceptability—are well positioned to tap into new revenue opportunities and potential penetration within the lending market.

In light of recent capital rule alterations globally, collateral flexibility and acceptability will likely remain key drivers of lending innovation over the near term.

As in many other areas, technology is also playing an important role in the evolution of our markets. Canadian providers continue to roll out advancements such as auto-borrow facilities, as well as a range of sophisticated mechanisms for enhancing transparency around portfolio data and client reporting.

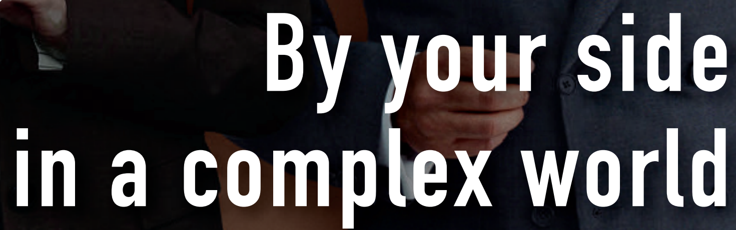
Advancements are also taking place in front-end systems and other areas are helping agent lenders deliver even stronger reporting, transparency and execution for participants.

Canada's owner clientele includes a wide range of leading public and private pension plans, many with three decades of involvement to their credit. These owners continue to view lending as a viable approach to offsetting custody costs while also generating incremental alpha, using services that can be tailored to meet their specific needs.

With fixed-income yields still trailing historical averages (particularly in Europe), investors continue to seek risk-adjusted returns and cost efficiencies across their businesses. On the demand side, borrowers are responding to mounting pressure around new clearing rules and liquidity/capital requirements, and considering treasuries-for-term and other arrangements involving high quality liquid assets.

All in all, Canadian securities lending can be expected to continue to gain traction among pension plans and other institutional participants seeking additional sources of alpha or to offset costs.

For beneficial owners that wish to capitalise, Canada's securities lending markets make a compelling argument. We are looking forward to hosting market stakeholders from around the world for what has become the Canadian industry's premier event, as we host the fifth annual Canadian Securities Lending Association conference in Toronto on 13 June. **SLT**



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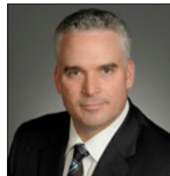
Lending alliances

Lacking liquidity? Canada is here to help. Securities lending experts discuss how

Dave Sedman
Head of Canadian securities lending
Northern Trust

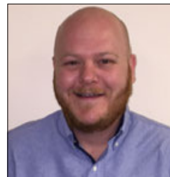
Nathalie Bockler
MD and head of securities finance and delta one sales, Americas
Société Générale

Charles Murray
Vice president and head of securities finance in Canada
State Street



Phil Zywot
Managing director securities finance
BNY Mellon

Alexa Lemstra
Head of Canada
EquiLend



Mark Dugdale
Editor
Securities Lending Times

How would you describe the last 12 months for the Canadian market?

Dave Sedman: Utilisation rates grew throughout 2014 while fees remained flat. Demand for Canadian equities was largely driven by dividend yield enhancement trades, dividend reinvestment plan (DRIP) trades and specific directional names. The DRIP trade continued to produce attractive returns and was a large driver of revenue for our clients. Borrower demand for the DRIP trade continued to provide a significant source of revenue, however, in the wake of lower crude oil prices, most of the oil and gas sector companies discontinued their DRIP offerings for the fourth Q4 2014.

> “Zywot: Increased spreads anddemand, especially on the Canadian fixed income side, has in turn led many beneficial owners to expand participation in lending of their Canadian fixed income supply”

Structured collateral upgrade trades with equities pledged as collateral also remained popular. Northern Trust also experienced a significant growth in revenue for equity loans with equity as collateral.

In response to regulatory changes, borrowers continued to pursue trading strategies that resulted in more efficient use of balance sheet. These include term-funding transactions and the use of a broader range of non-cash collateral types. With the need to satisfy new financial regulations imposed by Basel III and the Dodd-Frank Act (which requires banks and institutions to hold longer term financing), demand increased substantially for term borrows.

Charles Murray: The Canadian securities lending market—like others—has shifted focus in the last year, with a much greater emphasis on viewing opportunities through the prism of regulation, including the need to optimise capital usage. Generally, we’ve seen lower equity deal flow and fewer specials than in prior years. On the other hand, a greater focus on Basel III and liquidity coverage ratio and net stable funding ratio requirements have created new opportunities for collateral upgrade and term trades for those able to transact.

Nathalie Bockler: The Canadian market has been influenced by the volatility/decline in oil prices and observed in the foreign exchange rate. The TSX has lagged, while globally markets have rallied.

Phil Zywot: The Canadian market has seen healthy growth over the last year, reaching record balances—most notably in the fixed income area, which has set high water marks for each of balances, spreads and specials based on liquidity pressures. The reduced liquidity in the market has been reflected in the record amounts of overnight liquidity that the Bank of Canada has provided via its securities lending facility. Increased spreads and demand, especially on the Canadian fixed income side, has in turn led many beneficial owners to expand participation in lending of their Canadian fixed income supply. On the equities front, the market has remained steady, with the main driver of activity being the resource sector.

Canada has always been seen as a conservative market. Why is this and what does it mean for investors?

Bockler: I would not say ‘conservative’. Canada is well known for the high quality of its asset manager and pension investment professional communities. They are definitely prudent and apply thorough due diligence. When looking specifically at the securities lending market, the main difference with the US is the lower interest in cash collateral for ‘yield searches’. Transactions are viewed more on a risk/reward basis. I would add that Canadian investors were early adopters of asset swaps, or upgrade/downgrade transactions, as a means of increasing the yield on their assets.

Zywot: The conservative approach taken by Canada’s financial market participants and stakeholders gained considerable global attention during and following the 2008 market downturn, but has been the culture here for many years. Canadian participants tend to place a very strong focus on diligence, risk management and governance. For example, in terms of securities lending, these traits tend to manifest in an approach that focuses on achieving a risk-reward balance that is right for participants, as well as an appetite for clear and transparent reporting.

Our measured approach continues to be a key attractor for global investors seeking stability. Canada remains one of the few countries with a triple-A credit rating—one of the factors that drives so much demand for our government bonds.

Canada is also notable for the collaborative approach taken by the country’s regulators, releasing regulations well in advance and taking industry input into account, which, for example, led to the regulatory move to enable exchange-traded funds and real estate investment trusts to participate in lending activities on a level playing field with other types of investment fund structures. In securities lending and elsewhere, Canada remains a very attractive proposition.

Sedman: Canada is seen as a very stable market. Canadian banks are run conservatively with very healthy balance sheets and capital ratios, which are more than adequate with respect to Basel requirements. Additionally, Canadian government debt is AAA-rated. So one could understand how Canada may be viewed in that light.

> “Bockler: When looking specifically at the securities lending market, the main difference with the US is the lower interest in cash collateral for ‘yield searches’. Transactions are viewed more on a risk/reward basis”

However, I would argue that the Canadian market is quite mature and is starting to shed its conservative label. While it is true that Canada is a fairly ‘general collateral’ market, borrowers and lenders continue to look for new and more efficient ways to transact loans.

Borrowers are exploring collateral alternatives and trading structures, while lenders are earnestly trying to accommodate these requests. We are seeing an increase in requests for term trade and profit sharing structures, as well the expansion of acceptable collateral.

> “Murray: Alternative forms of collateral have gained importance and popularity as beneficial owners have seen value in the premium available for accepting non-traditional collateral”

Murray: Non-cash collateral has always been dominant in the Canadian securities lending market, unlike, say, the US market, in which cash has been the predominant form of collateral and cash reinvestment returns were a material part of lending programmes' total return. For years, the conservative nature of the Canadian market was highlighted by its lack of focus on reinvestment yield as a component of total return. In the past decade, however, cash collateral has played a larger role.

Additionally, alternative forms of collateral have gained importance and popularity as beneficial owners have seen value in the premium available for accepting non-traditional collateral, including equities, corporate bonds, exchange-traded funds and convertible bonds. While lenders are not materially changing their programmes' risk profile, collateral is increasingly being viewed as part of an asset-liability portfolio, where correlations to underlying loans are considered.

Why does Canada have such high participation rates in securities lending?

Zywot: The global regulatory environment continues to give rise to new and expanded requirements for global participants, in particular by significantly driving up the demand for high quality liquid assets (HQLAs). As a result, highly rated Canadian government bonds have been much in demand, and are likely to continue to see greater uptake.

We also see high participation rates among beneficial owners: many Canadian funds are sophisticated, experienced and well-established players that see securities lending as an opportunity to offset custody costs and generate strong risk-balanced returns in a persistently low interest-rate environment. Strong market uptake helps create additional momentum, as players that might otherwise stay on the sidelines take confidence from the Canadian market's very strong historical track record as well as their peers' success in participating in lending.

Murray: Canada has a mature securities lending market that has thrived for more than three decades. High participation rates are the combined result of the market's custody lending agents' extensive experience in securities finance markets and beneficial owners' comfort with securities lending. The latter acknowledge the incremental returns that can be achieved, with relatively low risk taken.

Custodial lending arrangements have also become more customised to lenders' needs in recent years. Minimum spreads, alternative collateral, enhanced risk management and reporting have all helped to maintain high institutional participation rates.

Sedman: Securities lending participation in Canada is high because Canada is a very stable and mature market and Northern Trust partners with a very sophisticated and educated client base. Participation in a securities lending program is one way for these clients to take advantage of borrower demand and increase the intrinsic value of their holdings, while earning incremental revenue. Many Canadian clients take comfort that securities lending provides is a lower risk investment strategy as the majority of loans in Canada are collateralised with non-cash collateral.

Additionally, we work closely with our clients to customise their securities lending programmes to meet their individual risk and return scenarios through a programme that is tailored to their needs.

Bockler: Canada also has straight-through processing (STP) opportunities and settlement in the Canadian Depository for Securities. This infrastructure is less developed in some countries. In addition, the simple size of available assets is important to the securities lending industry—the Canadian pension market is ranked fourth worldwide with assets under management of more than $1.2 trillion.

What drives cross-border activities?

Zywot: Cross-border activity stems from the large number of Canadian stocks that are inter-listed on US exchanges, as well as the non-cash collateral flexibility of Canadian beneficial owners. Canadian fixed income assets are highly sought-after forms of AAA-rated collateral, and we have seen an increased demand for Canadian product to meet global collateral demands.

Demand also stems from the International Monetary Fund's (IMF) 2013 addition of the Canadian dollar as an official reserve currency in 2013. As a result, many foreign central banks and sovereign wealth funds have moved to expand their Canadian holdings.

Sedman: Cross-border activities are driven by a variety of factors such as securities trading special, collateral upgrade trades, yield enhancement trading, and mergers and acquisition activity. Over the past year, two large Canadian companies (Amaya Gaming Group and Encana Corporation) have acquired cross-border companies, which resulted in an increase in demand from borrowers as well as an increase in fees.

> “Sedman: Cross-border activities are driven by securities trading special, collateral upgrade trades, yield enhancement trading, and M&A activity”

Murray: While European dividend-related trading activity has been a traditional source of cross-border activity, an increasing amount of borrow activity is being driven by regulatory requirements. Demand for HQLAs such as Canadian government bonds has increased, from both domestic and foreign sources. Those lenders with the broadest collateral and term parameters have derived the greatest benefit from this trend, with the ability to capture higher premiums.

Bockler: Cross-border activities in Canada are driven by a combination of implied index future levels, cross currency and global funding demand.

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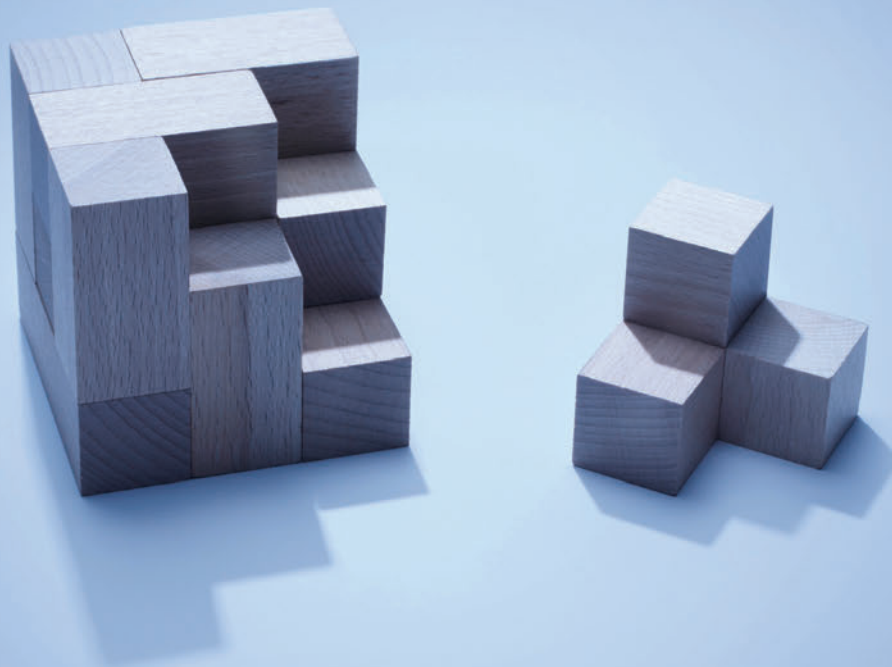

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What are the current trends in collateral?

Sedman: The majority of loans in Canada are collateralised by non-cash collateral as opposed to cash. However, in response to the evolving regulatory environment, borrowers continued to pursue trading strategies that result in more efficient use of balance sheet. This includes the use of a broader range of non-cash collateral.

Bockler: Financial institutions globally have become more and more constrained in balance sheet consumption. As a result, we observed a strong move towards non-cash borrowing and collateral upgrades. This is observable globally and in the Canadian market.

Zywot: In the past, the Canadian collateral market showed significant differences from the US approach. Canada was characterised by non-cash collateral, specifically sovereign debt, as opposed to the US market, which was predominately a US cash collateral market. In recent years, the two markets have converged with a move towards more cash collateral in Canada, and a move into non-cash collateral in the US. Canada is still an 80 percent non-cash collateral market, but we are definitely seeing a trend of lodging equities as collateral as borrowers look towards collateral and a focus on efficient balance sheet usage.

With the new regulatory framework, the Canadian securities lending space is seeing the term lending of HQLAs continue to gain importance in keeping with the global focus on deploying the right collateral.

CCPs continue to move along. Have there been any major developments or uptake in this area?

Murray: Central clearing has been a discussion topic within the industry for the last several years. Over the past year, with some of the recent regulatory changes having started to impact market participants and diminish capacity to conduct business at existing levels, there has been a renewed focus on the potential for some form of central clearing model to offer value in the securities lending space.

Both borrowers and agent lenders would expect to see certain benefits in terms of meeting regulatory requirements, including a reduction in the capital needed for conducting financing activities for their clients, which would help to preserve current flow and demand.

While most of the central clearing models that exist today are still challenged in terms of being able to service various parts of the industry, the level of engagement on the topic has been increasing and our expectation is that market participants will continue to explore the potential role for central counterparties (CCPs) to play in the future.

Bockler: Unlike the US, swaps are currently not centrally cleared in Canada. We expect a push from banks for a CCP in the future to mitigate credit and operational risk.

Zywot: CCPs have seen renewed interest as a potential distribution channel for agent lenders,

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in part to the regulatory changes that have been proposed. For example, in February 2015, BNY Mellon announced the formation of a joint venture with State Street and Eurex Clearing to collaborate with Eurex on a securities lending CCP solution.

In comparison to other mature markets, how efficient is the Canadian securities finance business?

Alexa Lemstra: Automation has come a long way in five years. There is a definite technology investment by the market participants in new systems to further efficiency. Canada had to grow in these areas to interact with the other mature markets globally and is a strong global player. We have experienced growth in the EquiLend client base, showing an interest of the Canadian market to focus on automation and STP for their businesses.

New clients continue to approach us for data, trading and post-trade services, and existing clients are looking to leverage our services more.

Sedman: The Canadian market continues to become more efficient and automated. Although not all market participants are completely automated, most are quite advanced from a technology standpoint. Many counterparties utilise AutoBorrow, STP, mark-to-market, Contract Compare and billing automation functionality.

Northern Trust continually invests in technology to ensure that we are at the forefront of automation and execution, and we encourage all of our counterparties to continue advancing toward a more efficient and automated market.

Murray: The Canadian market has made great strides in improving efficiency through automation. While it still lags behind the more developed US market in adoption of STP, there has been a noticeable change in focus to automation and digitisation. Pricing transparency has improved via the wide use of third party benchmarking services, which is visible to client lenders as well as agents and borrowers.

Zywot: In keeping with its generally conservative approach, it's no surprise that Canadian market players often prefer to implement proven technologies and incorporate lessons learned in other jurisdictions.

Nonetheless, Canada has recently moved to bring in a number of enhancements to improve efficiencies—for example, technologies such as AutoBorrow, Contract Compare, and triparty collateral facilities. Current execution rates reflect an efficient, transparent and mature market in Canada.

Do you see more automated trading in Canada, manual trading or a combination of both? Is anything else changing on the technology front in the market?

Lemstra: There will always be a need for traders to negotiate and arrange the deal names. Automation is predominately in place

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for general collateral trading to handle the low-touch, high-volume trades.

That said, with the recent release of Next Generation Trading (NGT), traders will have the ability to automate warmer trades, which we expect in Canada and other markets.

In Canada specifically, we're working with clients here to leverage NGT's robust trading capabilities that allow users to conduct their entire trading workflow on a single screen. It is designed to leverage the low-touch automation of STP while allowing traders to trade non-general collateral names in a centralised, easy and fast screen.

Also, market data has become more prevalent in the industry in Canada as firms look to integrate more data analysis and automation into their trading decisions.

Zywot: Automation continues to play an increasing role in the Canadian market. In the current market environment, there is significant focus on efficiency, which has in turn strengthened usage of technology platforms that help participants effectively move forward while meeting stakeholder needs.

In particular, we have seen increased volumes and activity in the AutoBorrow space. Providers are also working to hone their offerings to meet participants' growing demands around flexibility, connectivity and execution.

We have also seen an increase in the use of Contract Compare as it has helped deal with Canada's recent record volumes. Transparency continues to improve with recent new market entrants, and advancements in front-end systems continue to improve and streamline securities lending processes.

Murray: Automated trading in Canada will continue to gain acceptance as more and more players adopt automated platforms that can handle larger flows.

Of course, some percentage of trades will continue to be manual in order to allow for the evaluation of specific opportunities.

Sedman: Over the past year, there has been an increase in automated trading in Canada, especially in the autoborrow space.

Although there is still a decent amount of manual trading, the percentage is decreasing.

Most of the increase in AutoBorrow activity is directly tied to general collateral loans.

> "Lemstra: In Canada, we're working with clients to leverage NGT's robust trading capabilities that allow users to conduct their entire trading workflow on a single screen"

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As these trades are automated, it frees up our trading professionals to focus on securities with the highest intrinsic value.

From a client perspective, Northern Trust continues to make a number of enhancements to our securities lending technology, such as enhancements in reporting, to provide clients with transparent securities lending programmes.

How do you see the rest of 2015 panning out?

Murray: We expect 2015 lending volumes to remain on par with 2014 performance. Dividend yield enhancement trades, along with the DRIP trade, are expected to continue to generate significant interest and revenue for Canadian equities. General collateral volume will likely fall due to borrower balance sheet pressures.

Borrowers will likely focus on balance sheet friendly trades such as equity-for-equity or term, and will look for a broader range of non-cash collateral in order to keep pace with new regulatory requirements. Collateral will likely remain one of the key evolving areas within the Canadian securities lending market.

There may be consolidation in the energy industry during 2015. The 45 percent plunge in crude in 2014 made smaller producers vulnerable to larger buyers both in and outside of Canada, leading to potential mergers and acquisition activity and directional demand.

Sedman: I think the rest of 2015 will continue along the same lines that we've seen recently—steady, but with continued pressure from regulatory changes. Lenders, and their agents, that can be flexible and creative in terms of matching the needs of the demand side of the market will see good opportunities.

Lemstra: We are working with Canadian market participants to build out STP for NGT. We anticipate more traction and trading on NGT as clients in Canada and elsewhere realise the benefits of streamlined trading on the platform. We are also in active discussions with several market participants in Canada about joining the platform for data, trading or post-trade services.

Bockler: The financial industry will continue to focus on regulation, collateral management, cross-asset solutions and risk management.

Zywot: In 2015, I think we can expect to see a continued demand for Canadian AAA-rated debt as well as a continued focus on regulatory change, balance sheet and use of capital. The Canadian equity offerings trend is expected to continue—in the first quarter, it surged up to 86 percent year-over-year, and worldwide mergers and acquisitions activity was up 21 percent. The rest of the year looks bright indeed for securities lending participants and stakeholders. **SLT**

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Canadian securities lending: by the numbers

Canadian equities are keeping up their momentum in the securities lending market, says DataLend director Chris Benedict

Canada has maintained its position as the number two securities finance market in the world (behind the US) with an on-loan balance for equities of $107.87 billion at the end of last year, up 22 percent from year-end 2013. Canada continued to beat other big markets such as France, Germany, Japan and the UK.

We can see by the fee bands as a percentage of on-loan value (see Figure 1) that Canada's securities lending market reflects the stability of its overall economy. In general, fees to borrow Canada's equity markets were approximately 70 to 80 percent general collateral from 0 to 20 basis points, 5 to 10 percent warm in the 20 to 50 basis point range, 5 to 10 percent warmer or hot (50 to 500 basis points) and a very small percentage (roughly 2 to 3 percent) very hot, trading above 500 basis.

The hottest sector in Canada for 2014 was the industrials sector with a volume-weighted average fee (VWAF) of 59 basis points for the year. Industrials reached a peak of about 86 basis points in mid-August 2014 and ended the year at around 43 basis points, where they have remained for the first half of 2015.

Healthcare came in as the second warmest sector in Canada last year with an average VWAF of just under 50 basis points in 2014. A few hot stocks helped to push the Canadian healthcare sector higher, including Aeterna Zentaris, Oncolytic Biotech and ProMetic Life Sciences.

Finally, the materials sectors appears to be the third warmest sector in Canada with a VWAF of 41 basis points, pushed higher by an overall selloff in mining firms last year.

Despite the stable nature of the Canadian securities lending market, there were several names that were very actively traded last year. Westport Innovations was one of the most shorted stocks in Canada in 2014. Low oil prices, fluctuating exchange rates, sagging sales, a climbing debt-to-equity ratio and the acquisition of Netherlands-based Prins Autogassystemen Holding BV were all potential causes of this security selling off hard, losing 75 percent of its market capitalisation in a year.

In the securities lending market, it was in constant demand. With a VWAF of 934 basis points and average utilisations more than 50 percent, securities lenders made more than $3.31 million in this name alone last year. Westport recently was still trading at a VWAF of more than 4,300 basis points, making it one of the hottest names in Canada today.

Westport may have been one of the most shorted Canadian stocks of 2014, but the hottest stock award goes to Ballard Power Systems. The fuel cell maker had a daily average VWAF of 1,670 basis points and a daily average utilisation of more than 50 percent. Securities lenders made more than $2.1 million lending this name last year. Ballard Power Systems was still trading hot more recently with a VWAF of more than 1600 basis points and a utilisation of 71 percent.

Uranium Energy was a close second to Ballard in terms of how hot it traded last year. Uranium Energy yielded an average VWAF of 1,582 basis points and a 61 percent utilisation last year, earning securities lenders an estimated $1.85 million. Uranium Energy also remains very hot, commanding 1,500 basis points in fees recently with a 61 percent utilisation.

Once again, the Canadian market appears to be steady-as-she-goes, just as it did in 2013, with the proportion of hot trades thinning out again, while general collateral trades still dominate. Thus far, 2015 looks to extend that trend. **SLT**

Figure 1: Fees to borrow Canadian equities as a percentage of on-loan, January 2013 to May 2015

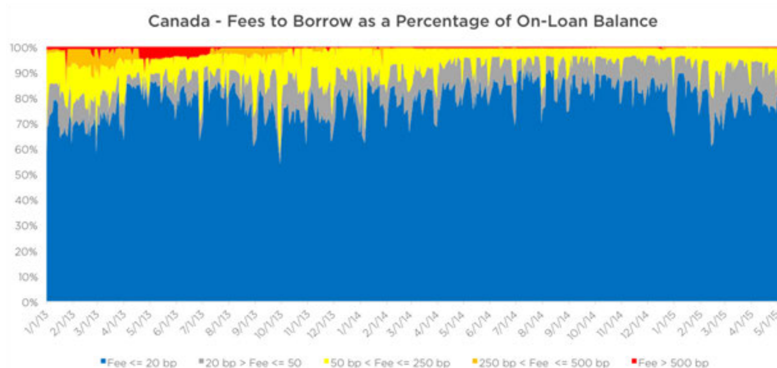

Figure 2: Volume-weighted average fees warm sectors, 2014 to 2015. Source: DataLend

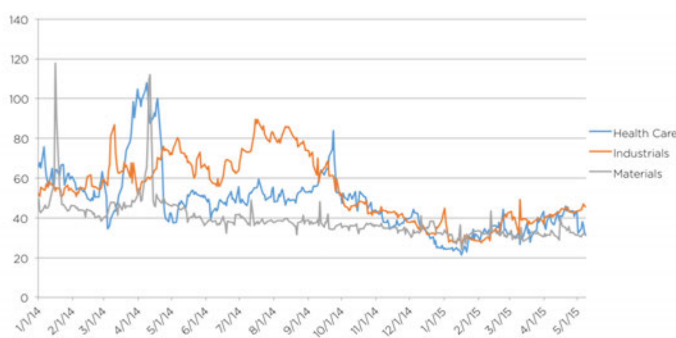

Figure 3: Volume weighted average fees by sector, 2014. Source: DataLend

Sector	VWAF (bps)
Industrials	58.83
Healthcare	49.77
Materials	41.33
Consumer Staples	26.47
Utilities	25.69
Information Technology	24.45
Energy	21.62
Consumer Discretionary	21.48
Financials	13.98
Telecommunication Services	10.57

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Anything that can go wrong, will go wrong

The ECB has had to make unexpected corrections to the course of its QE programme. David Lewis of SunGard's Astec Analytics takes a look

The law of unintended consequences is a difficult animal to manage indeed. The European Central Bank (ECB) began a quantitative easing (QE) programme, in effect 'printing money' to boost the momentum of the European economic recovery. The plan to purchase €60 billion quality European debt a month under the public sector purchasing programme (PSPP) is expected to last 18 months, at least initially. There are many arguments both for and against such a policy, but what of the perhaps unintended consequences?

Buying up so much debt each month (or around €1.1 trillion over 18 months) means that those bonds are no longer accessible by the market for whatever purpose, such as financing or collateral. To counter this, the ECB has introduced a securities lending facility to allow each national central bank (which is responsible for managing their relative shares of the ECB programme) to release those same bonds back into the market, commencing 2 April 2015. The objective of this programme is to "support bond and repo market liquidity without unduly curtailing normal repo market activity"—a laudable but difficult objective to manage.

Perhaps the comparison is an unkind one, but those of us of a certain age and of a certain disposition towards offbeat humour may remember The Hitchhiker's Guide to the Galaxy by Douglas Adams (look it up if you don't know it). Towards the end of the story, a small group of humans who have survived the destruction of Earth attempt to colonise a new planet and decide tree leaves would form a suitable currency. They then had to commence a major and urgent deforestation project to counter the hyperinflation that resulted from the sudden abundance of liquid currency.

Not a perfect analogy, but not dissimilar in a sense of taking one action to fulfil an objective and then having to take a potentially unexpected course of action to cope with the unintended and potentially disastrous effects.

But what is the effect in the real world of the markets? Has the pulling of various levers by the ECB caused a ripple or a tsunami in the European collateral pool? The laws of supply and demand affect all markets; repo and securities lending are not immune and the need for high quality liquid assets for collateral and regulatory purposes is indeed pushing up the borrowing costs for specific securities that are in demand. Certain parts of the curve for German bonds are already in negative yield territory as investors effectively pay the German government to hold this paper. According to Bloomberg, 67 percent of its Germany Sovereign Bond Index is yielding less than zero. The ECB QE programme sucking additional liquidity out of the financing market will only add to the pressure on the supply of specific 'special' securities.

The ECB's new lending programme (the part of the analogy where they burn all the trees) will allow the participating central banks to lend out securities for a set fee of 40 basis points—some four times the rate currently charged in the securities lending market for German government bonds, according to our figures. While this service remains this expensive, it will not be used by the market to plug any liquidity gaps and may even drive additional demand in the cash market for the more desirable securities, which will push further debt issues into negative yields.

Figure 1 shows the volume and intrinsic fee rates for the European government bond market over the last nine months. The PSPP came into play on 2 April this year and, given the assumption above regarding the repo market and setting an effective ceiling for borrow rates, it is not surprising that there is no discernible bounce in fee levels for either European government bonds as a whole, or more specifically, the German bond market.

What is interesting, however, is the general trend in rates. Ignoring some choppy moments in January and February, the general trend is a slow increase in the fee levels being charged for high quality liquid assets. The other striking, although perhaps not too surprising, characteristic of this graph is the correlation between the wider European market levels and that of the biggest market, Germany.

Extrapolating this trend suggests it would take a very long time for the securities lending market average rates to get anywhere near the 40 basis point PSPP standard rate. With an expected duration of no more than 18 months, it is unlikely that the borrowers of even special government securities are going to trouble the ECB's liquidity support service too much, thereby leaving all those juicy assets locked away in the central banks.

The lack of a significant upturn in borrow rates also suggests that the QE asset buying programme is not yet testing the ample levels of supply in the market. Inventory information we hold here in SunGard's Astec Analytics, together with more anecdotal evidence from agents and their beneficial owners, would suggest that the supply is not going to suddenly shrink any time soon, and with the ECB PSPP acting as a backstop source, albeit an expensive one, the sage words on the cover of the Hitchhiker's Guide come to mind—"don't panic". **SLT**

Figure 1: Average intrinsic borrow rates for European and German government bonds, nine months to 7 May 2015

David Lewis
Senior vice president
SunGard's Astec Analytics

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Industry appointments

David Linds is to retire from his role as senior vice president of business development and relationship management at CIBC Mellon on 1 July.

Rob Ferguson has also been appointed to the role of senior vice president of capital markets, business development and relationship management, while Richard Anton will become senior vice president and COO, with both appointments also effective on 1 July.

Linds has been with CIBC Mellon since its inception in 1996, and has led the bank's sales and relationship management functions for more than a decade.

"A leader throughout CIBC Mellon's history, Linds helped grow the company to more than $1.5 trillion of client assets under administration from $100 billion over the past 16 years," said Tom Monahan, president and CEO of CIBC Mellon.

"[His] leadership, insights and relationship skills have been invaluable throughout the company's journey, and his passion for the business and for our clients is a point of great admiration across the firm."

In his newly created role, Ferguson will take on overall responsibility for building and strengthening CIBC Mellon's relationships with clients across the asset servicing spectrum.

Ferguson has 25 years of industry experience, having also joined CIBC Mellon at the bank's inception.

His prior roles at CIBC Mellon include vice president of product and client service, co-head of global securities lending, and, most recently, senior vice president of capital markets and product delivery.

With his appointment to the role of senior vice president and COO, Anton will continue to lead CIBC Mellon's client service delivery teams, while also taking on responsibility for the bank's corporate project office, product management and centralised client administration functions.

Anton joined CIBC Mellon in 2014 in the role of vice president of operations and has nearly 20 years of financial industry experience.

His former roles include serving as chair of the board, senior vice president and COO at State Street Cayman Trust Company, and as a member of the board of directors for State Street Fund Services Toronto.

Mizuho Securities has hired William Wong to expand its securities lending and equity financing business in Asia.

Wong will report to PJ Andersson, head of equity (excluding Japan) at Mizuho Securities Asia, and Tomoaki Kinoshita, head of pan-Asia equity finance at Mizuho Securities Tokyo.

Wong previously worked for Macquarie Securities in Hong Kong.

Ted Langworthy has joined SEB as senior sales trader, within the hedge fund sales trading group, in New York.

Langworthy will report to Marcus Segersten, who runs hedge fund sales trading globally.

He joins SEB from HSBC's New York office, where he was director and distributed equity financing and delta one products to North American hedge funds active in international equity markets.

Prior to that, he spent three years as head of non-US equity financing for the Americas at Deutsche Bank in New York.

Head of Asia Pacific equities at Deutsche Bank, Dixit Joshi, is to assume the role of global head of prime finance and move to London, according to reports.

Joshi will replace Barry Bausano, who is set to become chairman of hedge funds, serving as an adviser to clients, as well as continuing to serve as president of Deutsche Bank Securities.

The move follows the departure of Murray Roos, who recently took the role of global head of sales for Citi's equities and prime finance divisions.

Roos spent eight years at Deutsche Bank in a variety of senior management positions, most recently as global co-head of prime finance and co-head of European equities.

In his newly created role, Roos will be responsible for developing and leading a unified and global sales strategy across the full range of equity and prime finance products offered to Citi's clients.

He will be based in London and report to Derek Bandeen, global head of equities, Okan Pekin, global head of investor services, and Jim O'Donnell, global head of investor sales. SLT

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