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Consolidation is highly likely, according to BNY Mellon and The Field Effect

New regulations and changes in financial markets mean consolidation in collateral management is highly likely, according to a report from BNY Mellon and The Field Effect.

The new report, Collateral Management: A Review of Market Issues, argues that consolidation is "a highly likely outcome" and collateral management will evolve from being primarily a process of managing assets for margin purposes, to a position where much greater consideration is required to manage assets.

The possibility of a shortfall of market collateral, potential changes that firms can make to existing account structures, systems and services, the role of third-party service providers in helping market participants to manage collateral effectively, and the future shape of collateral management are all discussed in the report.

Key challenges in collateral management identified by the report include compliance with new regulations governing cleared and non-cleared over-the-counter derivatives.

The buy side is also under pressure to choose partners that can support complex requirements for margining and collateral mobilisation, while banks will have to meet complex interlocking collateral and capital regulations at the same time as offering customers collateral services at a viable price point.

The ability of custodians to provide customers with a cost-effective collateral management service with integrated triparty capabilities will also be tested, according to the report.

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SmartStream upgrades TLM Collateral Management

SmartStream has launched a TLM Collateral Management adaptor to provide a full lifecycle of trading messages for the non-clearing over-the-counter (OTC) derivatives market.

The new adaptor to TLM Collateral Management, which SmartStream acquired from IBM in February, will integrate the system with ArcadiaSoft's Margin Sphere clearing services.

SmartStream is providing full coverage of the lifecycle messages and events supported under STP, reducing the need for ad hoc manual activities at other terminals.

The adaptor was delivered as part of SmartStream's latest release of TLM Collateral Management v5.2.10.

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New benchmark index for ECB

The European Central Bank (ECB) will now use Deutsche Börse Group's STOXX EUR GC Pooling index as its new benchmark rate for fixed term deposits, following the discontinuation of the Eurepo index.

The secured market rate with regard to fixed term deposits in euro will be the STOXX EUR GC Pooling term indices with a comparable maturity, according to the ECB.

STOXX EUR GC Pooling indices are calculated by STOXX, the global index provider that is owned by Deutsche Börse Group. The indices are based on secured euro funding transactions taking place on Eurex Repo's GC Pooling market, Deutsche Börse's pan-European marketplace for international financing in the secured money market.

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Collateral management likely to consolidate

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Mark Higgins, managing director in the markets group at BNY Mellon, and one of the co-authors of the report, commented: "The development of an effective collateral management solution is a complex combination of market variables, many of which continue to evolve. We believe those firms who fail to master the fundamental strategic collateral questions will find themselves at a considerable disadvantage."

"Banks may find themselves unable to fund core business lines or meet the needs of clients cost effectively, while asset owners and managers may find themselves unable to pursue preferred investment strategies. Whilst there is consensus that the subject area is complex and in flux, it is also clear that considerable prizes are available for those who identify their specific collateral service elements and requirements."

David Field, founder and principal at The Field Effect, added: "Asset managers, pension funds, insurance companies, banks and broker-dealers face complex regulatory and market structure changes. This task should not be underestimated and many firms may not fully appreciate the challenges they face, nor recognise the opportunities available in the market."

"As the sophistication of collateral services evolves, we will see increasing levels of innovation from service providers who truly understand their clients' needs and have the vision to develop services to support them. A critical part of the collateral challenge will be for firms to select the service elements they require and identify the service provider that can most effectively meet their needs in the long term."

SmartStream upgrades TLM Collateral Management

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SmartStream has developed the adaptor in response to International Organization of Securities Commissions (IOSCO) and Basel Committee risk mitigation standards for the non-clearing OTC derivatives market, which require trading desks and collateral managers to understand which assets should be preserved for use as collateral and which, potentially, are available for trading.

Darryl Twiggs, head of product management at SmartStream, commented: "Volumes in non-clearing OTC are predicted to rise by a factor of ten in 2016 following the implementation of new IOSCO regulations for intra-day margin call calculations."

"I am delighted that we have been able to use our TLM technologies to deliver the adaptor quickly. This brings collateral management closer to our other solutions in portfolio and margin settlement reconciliations and intra-day funding liquidity management."

He added: "The challenges further increase when firms are engaged in derivatives activity through a variety of legal entities in different national jurisdictions; we are speaking to clients who are seeking to mitigate risk in derivatives for cross-border transactions."

New benchmark index for ECB

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Almost all of European interbank financing is now executed on a collateralised basis. STOXX and Eurex Repo jointly developed the STOXX GC Pooling indices in 2013 as a market barometer of Europe's largest secured money market, GC Pooling, according to Deutsche Börse.

"We are very pleased that the ECB is going to use our STOXX EUR GC Pooling indices as it validates our approach and concept," said Hartmut Graf, COE of STOXX.

"Our transparent, rules-based and reliable benchmark for the interbank market contributes to regain trust in reference interest rates."

Marcel Naas, managing director of Eurex Repo, added: "Our GC Pooling market is a regulated, anonymous, and centrally cleared marketplace

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with an average daily outstanding volume of more than €150 billion.”

BSC enters US market

The BSC Financial Group has acquired Alforma Capital Markets, the New York-based subsidiary of Alfa-Bank.

The move will allow BSC to break into the North American market by taking full control of the broker-dealer, pending the approval of US regulators.

The US Securities and Exchange Commission and the Financial Industry Regulatory Authority are expected to approve the purchase by the end of 2015.

The company will be re-branded as BCS Americas under the continued leadership of CEO, David Denson.

The subsidiary will provide brokerage and investment services to US-based institutional clients looking to access Russian markets.

BSC is the largest securities broker on the Moscow Exchange, currently controlling 25 percent of securities trading across all asset classes.

Roman Lokhov, CEO of global markets and investment banking at BCS, said: “Despite the temporary geopolitical challenges, US-based institutions remain the leading international investors in emerging and Russian assets.”

“Therefore we see huge potential in the US for our business to seize significant market share.”

“We expect the macro and geopolitical conditions in Russia to recover eventually, and believe this is the right time to invest in our ability to service the US and expand our platform.”

LCH.Clearnet to use SWIFT for margin calls

LCH.Clearnet plans to use SWIFT to notify clearing members of margin calls from November.

The clearinghouse already uses SWIFT to send and receive collateral messages with its members.

Under the new process, LCH.Clearnet’s members will receive margin call notifications faster and in a standardised format, increasing operational efficiency and straight-through processing (STP).

The messages will comply with ISO 20022 MX standards.

The service was developed in collaboration with SWIFT and the global ISO standards evaluation group. It will also be available to members of LCH.Clearnet LLC.

Gerard Smith, director of collateral Services at LCH.Clearnet, said: “We’re committed to improving efficiency for our members, and we have developed this new service with them in mind. Leveraging SWIFT enables members and their clients to be notified of their margin obligations in a more timely and standardised fashion.”

“We’re delighted to have collaborated with SWIFT to be the first CCP to offer this service to our members and their clients.”

Arun Aggarwal, head of UK, Ireland and the Nordics at SWIFT, said: “LCH.Clearnet’s adoption of ISO 20022 standards for these margin calls is a great example of the market moving towards greater standardisation and efficiency.”

He added: "We're pleased to be working with LCH.Clearnet to deliver a fast and effective way for members to receive notifications of margin calls. This forms part of SWIFT's wider global efforts to assist members with STP programmes for collateral management."

Playtime's over for Mattel

Toymaker Mattel has increasingly attracted the attention of short sellers in the US since the end of 2014, according to Markit.

Short sellers have abandoned rival Hasbro and increased their interest in Mattel as investors have done the opposite.

Short interest in Mattel declined towards the end of 2014 as short sellers took profits and covered, but shares outstanding on loan have subsequently soared in 2015, rising almost five fold to 19.8 percent.

Mattel stock has fallen by 28 percent so far this year, while Hasbro shares have climbed 34 percent.

In Europe, Nordic Semiconductors has 8.6 percent of its shares outstanding on loan. Shares in the chipmaker have fallen by a third in the last 12 months despite strong sales and profit growth expected for the full 2015 financial year.

Elsewhere in Europe, short sellers are targeting French food and clothing retailer Rallye, which has seen a five-fold rise in short interest in the last three months with shares outstanding on loan standing at 7.9 percent.

Tokyo-based U-Shin, a manufacturer of products for the automotive and industrial sectors, is the most shorted in the Asia Pacific, according to Markit.

Its shares outstanding on loan tracking the share price higher. They have increased to 9.8 percent as shares have increased by a fifth in the last 12 months. The share price increase has in turn tracked a rise in sales and earnings at the company.

US SEC supports T+2 settlement cycle

An industry coalition has welcomed a letter from the head of the Securities and Exchange Commission (SEC) supporting the move to a two-day settlement cycle (T+2) in the US.

The T+2 Industry Steering Committee is pushing for a move to T+2 in the US to foster greater certainty, safety and soundness in capital markets, as well as reduce counterparty risk and procyclical margin and liquidity demand across the industry.

SEC chair Mary Jo White wrote to steering committee members the Securities Industry and Financial Markets Association (SIFMA) and Investment Company Institute (ICI) in September, saying: "For these and other reasons, it is in my view incumbent upon all segments of the securities industry, including, where needed, the regulatory community, to work together expeditiously on this important matter."

Tom Price, co-chair of the steering committee and managing director of operations, technology and business continuity planning at SIFMA, commented: "Obtaining regulatory support for the move to T+2 is critical and we applaud the SEC for their leadership and support in this major initiative to strengthen our financial system."

The steering committee is pushing for a move to T+2 in the US by Q3 2017. It issued a whitepaper in June outlining the proposed timeline and work that needs to be done to complete the project.

“Moving to a shorter settlement cycle will help improve the overall efficiency of securities markets, align the US with other global markets and promote financial stability,” reaffirmed Marty Burns, co-chair of the steering committee and chief industry operations officer at ICI.

The SEC, as well as other regulators and self-regulatory organisations, need to coordinate to implement or approve the regulatory changes that are required to support the move to T+2 in the targeted timeframe.

The steering committee also plans to begin developing industry test and implementation plans, and advises industry participants to begin assessing the work needed for internal builds.

Industry-wide testing is expected to begin in 2017 in support of the Q3 2017 implementation of T+2, according to the steering committee.

Eurex to launch improved margin calculator

Eurex Clearing will launch its new Prisma Margin Estimator (PME) on 16 November.

The service aims to enhance Eurex’s risk management services though a more sophisticated assessment of Prisma’s initial margins for current and hypothetical portfolios. This additional service was developed in close collaboration with OpenGamma, a financial technology company specialising in market structure risk management solutions.

“We have worked closely with Eurex Clearing to ensure that the Eurex Clearing PME supports their state-of-the-art margin methodologies and the needs of their clients,” said Mas Nakachi, CEO of OpenGamma.

“The Eurex Clearing PME is the latest example of our close work with the derivatives industry

to deliver much needed and enhanced margin analysis capabilities.”

Volume down in September at OneChicago

OneChicago’s volume in September was down 29 percent year-over-year to 964,510, according to the securities finance exchange, although it did increase 14 percent over the previous quarter.

Year-to-date volume through 30 September was 8,969,657, an increase of 13 percent over 2014.

Open interest, meanwhile, decreased 22 percent year-over-year to 528,736 contracts on the equity finance exchange at close-of-market on 30 September.

Month-end open interest of 49 percent was also in OCX.NoDivRisk products, according to OneChicago.

AI platform takes over ISDA CSA data extraction

CloudMargin has partnered with RAVN Systems to apply an artificial intelligence platform to the extraction of data from collateral agreements.

CloudMargin, using the RAVN Applied Cognitive Engine (ACE), will handle the

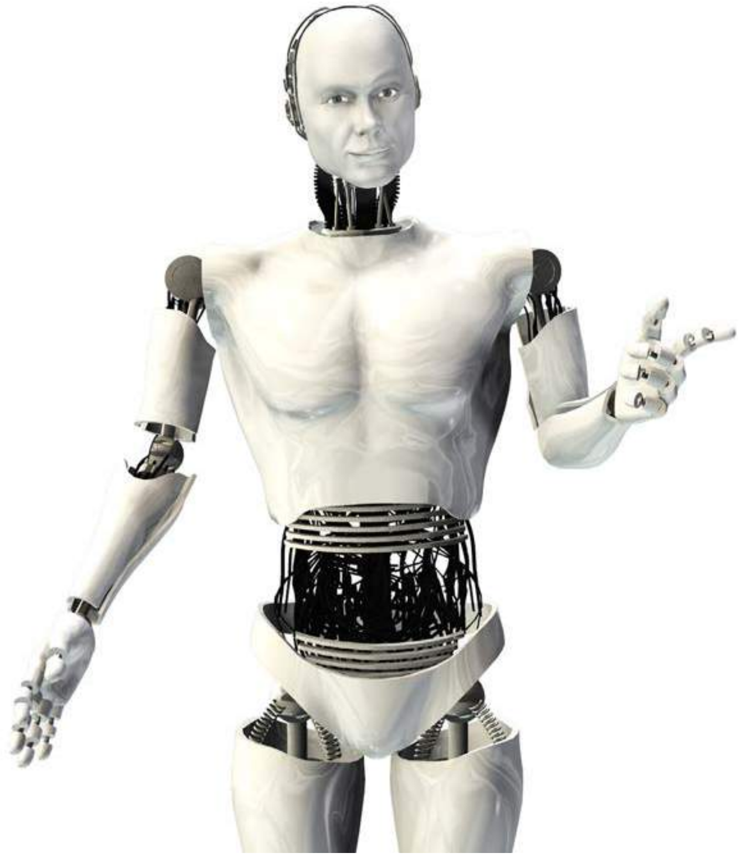
automated and secure data extractions of key terms from International Swaps and Derivatives Association (ISDA) credit support annexes and other collateral agreements.

RAVN ACE joins elements of artificial intelligence and information processing to deliver a platform that can read, interpret, extract and summarise the content held within ISDA credit support annexes and other legal documents.

The system will convert unstructured data into structured output, in a fraction of the time it takes a human and with a higher degree of accuracy, enabling CloudMargin to increase the analytical efficiency of client legal documents.

Peter Wallqvist, managing director at RAVN Systems, commented: "RAVN Systems are delighted with the partnership with CloudMargin."

"Repeating our collaborative approach with domain experts in the legal sector, we will use CloudMargin's expertise in business processes within financial services, together with RAVN's expertise in employing its cognitive computing platform, to derive structure from masses of unstructured financial documents."



SunGard platform wins UKAR treasury mandate

UK Asset Resolution (UKAR) has adopted SunGard's Ambit Treasury Management system.

UKAR, the holding company that combines the UK government-owned businesses of Bradford & Bingley and NRAM, aims to use SunGard's solution to consolidate the two businesses' infrastructures into a single treasury and risk system.

The solution will streamline treasury operations by integrating dealing, funding, position management and risk assessment of multiple asset classes into one system, according to SunGard.

Ambit will help UKAR to automate transaction flows across the front, middle and back offices, reduce manual processes, and gain a complete and accurate view of credit and market risk exposure.

ECB's quantitative easing policy hits Eurex's repo clearing

Eurex Repo recorded an average outstanding volume of €147 billion in all markets for September due to the European Central Bank's quantitative easing programme, according to Eurex Clearing trading statistics.

Eurex Repo, which operates the European repo and general collateral (GC) pooling markets, endured a €64 million drop-off compared to its September 2014 clearing data.

The wider European repo market only reached an average outstanding volume of €25.7 billion, compared with €42 billion in September 2014.

The secured money market GC pooling recorded an average outstanding volume of €121.3 billion, down from €169.4 billion in September 2014.

The international derivatives markets of Eurex, part of Deutsche Börse Group, recorded an average daily volume of 9.9 million contracts, 7.5 million of which were Eurex Exchange contracts.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The New York-based International Securities Exchange recorded 2.4 million traded contracts.

At Eurex Exchange, the equity index derivatives segment totalled 90.6 million contracts, compared to 68 million in September 2014.

The single largest contract was the future on the EURO STOXX 50 Index with 40.5 million contracts, and the options on this blue chip index totalled 31.5 million contracts.

Futures on the DAX index recorded 2.9 million contracts while the DAX options reached another 3.8 million contracts. The Eurex KOSPI Product recorded 2.3 million contracts.

OCC sees sec lending up by almost a third

New loan activity in OCC's securities lending central counterparty increased 29 percent in September over the same month in 2014.

Year-to-date stock loan activity is up 15 percent from 2014 with more than one million new loan transactions in 2015.

The average daily loan value cleared by OCC in September was valued at $193 billion.

Overall, OCC recorded a 3 percent drop off in cleared contracts volumes, compared to September 2014.

Cleared contracts fell from 371 million in 2014, to 361 million this year.

OCC's year-to-date average daily cleared contract volume also dropped by 0.17 percent from 2014.

"With lower levels of volatility, options trading volume decreased in September versus August, which is consistent with lower volumes in the underlying securities markets and index futures," said Scot Warren, executive vice president of business development at OCC.

Exchange-listed options volume was also down 3 percent and equity options dropped 6 percent from September 2014.

OCC cleared futures for September went against the trend entirely with a 32 percent increase on September 2014 figures, although year-to-date average daily cleared futures is down 0.25 percent from this time last year.

Irish UCITS reform streamlines repo and sec lending

The Central Bank of Ireland has simplified its requirements for UCITS funds.

The central bank published its updated requirements, which aim to consolidate all of the conditions imposed on UCITS, their management companies and depositories into a single document, on 5 October. They will come into effect on 1 November.

UCITS funds are ultimately governed by the EU but member states are allowed a degree of autonomy in their interpretation of the guidelines.

The reformed framework for Ireland has implications UCITS funds that engage in the securities lending and repo markets, with minimum liquidity requirements in stress scenarios and counterparty ratings.

It dictates that any counterparty involved in securities lending, repo or reverse repo transactions "must have a minimum credit rating of A-2 or equivalent, or must be deemed by the UCITS to have an implied rating of A-2 or equivalent".

"Alternatively, an unrated counterparty will be acceptable where the UCITS is indemnified or guaranteed against losses suffered as a result of a failure by the counterparty, by an entity which has and maintains a rating of A-2 or equivalent."

The central bank also highlighted the importance of ensuring the recall of securities is available to UCITS funds "at any time" to ensure liquidity is guaranteed.

Exposures created through the reinvestment of collateral must also be taken into account in the issuer concentration calculations.

In addition, the reformed framework removes the requirement for promoters of UCITS funds to be approved by the central bank and brings the approach for UCITS funds in line with that for alternative investment funds.

The reforms were welcomed by Irish Funds, the representative body for the cross-border investment funds industry in Ireland.

Pat Lardner, CEO at Irish Funds, said: "This is a positive development for the Irish funds industry, and the removal of the promoter approval will ensure the regulatory framework is accessible to the broadest range of managers/promoters."

Post-trade pair slash pending CAD IRS notional

TriOptima and SwapClear have eliminated 20 percent of inter-dealer notional outstanding in cleared Canadian dollar (CAD) interest rate swaps (IRS).

The post-trade service providers saw 18 clearing participants cut CAD $1.6 trillion (US $1.23 trillion) in LCH.Clearnet's SwapClear.

"Our last two cycles have eliminated CAD $3.3 trillion (US $2.55 trillions) in outstanding CAD IRS in SwapClear, contributing to a further reduction in systemic risk for the market and regulatory capital for individual institutions," said Michael Modlock, head of triReduce North America.

"We continue to see greater compression possibilities as unlinking trades in the central counterparty provides a larger pool of eligible swaps for compression."

As clearinghouses unlink trades from the original counterparty to create 'unlinked trades', dependency on the participation of other clearing members is reduced, resulting in a larger pool of trades eligible for compression, according to TriOptima.

TriOptima and LCH.Clearnet's SwapClear currently offer compression cycles for more than 10 currencies.

Vietnam considers short selling

Vietnam's two stock exchanges may soon allow short selling activity to begin, according to media reports.

The State Securities Commission is debating the reform as a way to boost liquidity and trading volumes in the market, a local media outlet reported.

A draft circular including the proposal on short selling is to be submitted to the Finance Ministry.

CloudMargin and REGIS-TR team up for EMIR reporting

CloudMargin has integrated REGIS-TR within its solution to offer automated European Market Infrastructure Regulation (EMIR)-compliant swap data repository reporting of over-the-counter derivatives.

This will have a “huge impact” on CloudMargin’s clients, which will now be able to adhere to EMIR-compliant trade reporting automatically, avoiding the need for further third-party solutions or middleware, according to CloudMargin.

REGIS-TR collects and administers details of transactions reported by CloudMargin’s clients, to give market participants and regulators an aggregated view of positions in compliance with current and upcoming regulation.

Its European Reporting Hub will also cover securities finance transaction reporting in the future.

Stuart McHardy, managing director and co-founder of CloudMargin, commented: “Thanks to this collaboration between ourselves and REGIS-TR, CloudMargin clients can rely on a market-leading solution for their regulatory reporting requirements, with this automated connection alleviating the stresses clients face when struggling to stay compliant in an ever-changing regulatory landscape.”

SS&C GlobeOp records dips

The gross return of SS&C GlobeOp’s Hedge Fund Performance Index for September 2015 measured -1.56 percent, down from the -1.02 percent in recorded in August.

Hedge fund flows as measured by the SS&C GlobeOp Capital Movement Index declined 1.13 percent in October.

Bill Stone, chairman and CEO of SS&C Technologies, explained: “SS&C GlobeOp’s Capital Movement Index for October 2015 was -1.13 percent, down from the previous month’s 0.62 percent, reflecting primarily seasonal factors.”

“Comparing year-over-year flows, the -1.13 percent for October 2015 was virtually identical to the October 2014 reading of -1.12 percent, with both inflows and outflows closely in line for the comparative periods.”

“We have been analysing our Capital Movement Index and Forward Redemption Indicator carefully in the wake of recent market volatility. October’s results are certainly indicative of overall stability in hedge fund allocations.”

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

Clearstream’s sec financing service dips for September

Clearstream’s global securities financing (GSF) services figures showed its monthly average outstanding dropped 8 percent in September.

The combined services include securities lending, triparty repo and collateral management saw its average drop from €632.2 billion to €581.3 billon between September 2014 and the same month this year.

Clearstream’s GSF monthly average outstanding did increase 2 percent, from €601.7 billion between January and September 2014 to €613.2 billion in the same period in 2015.


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Defining the rules

Andrew Dyson of the International Securities Lending Association discusses which regulations have been clogging up his desk this year

DREW NICOL REPORTS

ISLA has described the sec lending industry as heading towards an 'age of enlightenment'. Can you expand on what that means?

We are now at a point where we have a lot of regulations that are in-flight, currently being implemented or are about to hit our world. We know most of the detail behind the biggest regulations. There's nothing new expected from the regulators in the sense of how they manage and control visibility into our market. So as we go through the implementation phase, we will reach what Kevin McNulty and I refer to as the 'age of enlightenment', which means we have a very clear regulatory environment with a lot of transparency that allows the market to go back to focusing on what it's good at.

Having said that, there will always be updates to regulation because every now and again regulators need to see how well the existing framework is working and if it needs amending or tweaking.

What have been the major issues that ISLA has had to work through in the past 12 months?

There have been four substantial pieces of regulation that we've had to engage with over the last 12 months. The Central Securities Depositories Regulation (CSDR) will bring in mandatory fines and buy-ins, and we've consulted extensively on that.

The second is the Securities Financing Transparency Regulation (SFTR), which was brought in by the European Commission and finalised in June. There was a lot of work done in the run up to finalising the text, because some parts of the SFTR were quite hard on the market, but we did get some positive movement on those issues.

One of the biggest regulations is the rolling impact of Basel III, particularly the liquidity coverage ratio and the net stable funding ratio. We've done a lot of work on how those affect market participants and to see if there is any room for calibration of those ratios to make them more straightforward for securities finance.

Finally, we've been working on the implementation of the Bank Recovery and Resolution Directive, particularly the 'stay' provisions, which allow the regulators to suspend close-out rights under repo and securities lending agreements. Regulators already have, or are implementing, these powers at a regional level, but they've asked that those same powers be embedded in our agreements. It's a long and complex process but we have to work on it.

Would you say this year has been one of your busiest in terms of the sheer volume of regulatory consultations you've had to deal with?

That's fair. We've had six or seven big regulatory initiatives that we've responded to, either initial consultations or later in the process. We have had an ongoing dialogue with the Financial Stability Board (FSB) for two or three years. The CSDR in particular prompted a big response from us. At the same time, the rolling impact of Basel III, especially on broker-dealers, has resulted in a lot of engagement on our part. We have also done work on the capital markets union, UCITS, the Transparency Directive, the Markets in Financial Instruments Directive and the European Central Bank's Money Market Statistical Reporting.

Is it the busiest year ever? It's not far short.

Do you expect to be able to spend your time on other association tasks in the near future?

As an industry association, we're responsible for many things, such as creating best practice, industry training, running standard market documentation and working with regulators and policymakers to try and ensure we have sensible, pragmatic and workable regulation for our industry. While you would expect that final point to be a major part of our role, for the past two years it's pretty much dominated and, on occasion, that's all we do for weeks at a time.

We would like to think that in a year or two that balance will swing back and we can do more of the best practice, training and general market development activities you would expect us to do.

Finally, CCPs having been one of this year's hottest topics. What is ISLA's stance on using CCPs or their place in the securities finance chain?

When the FSB did its first report on shadow banking, it didn't suggest mandatory clearing for SFTs. Eurex Clearing does have a very well-developed central counterparty (CCP) model for our industry, which, because of the agency structure, is unique.

ISLA is quite neutral. We're happy to explain to market participants how CCPs work and what the potential issues might be and create forums for people to discuss these issues. We help to create visibility for CCPs around what our members are doing. The market will decide if it the time is right to use the CCP, based on many issues around economics and capital efficiencies. We're very supportive and believe it's a part of the market that needs to develop—there's inevitability there. SLT

Andrew Dyson
COO
International Securities Lending Association

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ETFs As Collateral

The Results

ETFs as collateral: are they your funding friend?

Why are ETFs growing in Europe but their use as collateral in securities lending is not? A Securities Lending Times and Markit survey reveals what the market is thinking right now, and how the use of ETFs as collateral can grow in the future

In this new world of collateralisation, securities lending is an old hand. Beneficial owners across the globe calculate risk against reward, and the indemnity their agent lenders can obtain from borrowers on their behalf is an important figure in that calculation. If the reward outweighs the risk, deals can be done. If that risk is too great, the beneficial owner will seek a borrower elsewhere.

The forms that this indemnification can take are myriad and complicated, each with its own pluses and minuses that weigh differently on the minds of the individuals concerned. Indemnification is subjective—what is wrong for one beneficial owner might be right for another.

The exchange-traded fund (ETF) is a form of collateral that is growing in stature, particularly in the US and Europe. According to Markit, the global exchange-traded product (ETP) industry stands slightly below $3 trillion in assets under management (AUM), after growth of more than 16 percent in 2014, with Europe contributing inflows of more than $61 billion and the US contributing inflows of more than $240 billion. Forecasts anticipate global AUM to more than double over the next five years, with Europe being an important driver of that growth. European assets are less than a quarter of US assets, although net inflow growth in European assets, relative to the size of the region, was higher in 2014 and continues to be higher in 2015.

Drilling down in to ETFs, Europe is catching up with the US. Markit ETF data show the US market is currently four times the size of Europe, and the reported turnover in US ETFs is seven times higher than the Europe, Middle East and Africa (EMEA) region. But growth in the US ETF market is starting to flatten, as inflows in the EMEA region grow faster than they do in the US. So, the US appears to have peaked, but Europe is working to catch up. Indeed, Markit notes that the EMEA has almost double the number of exchange-traded products of the US, while its bid/ask spread is approximately 50 percent higher than in the US on average.

It surprising, then, to see that as US ETF lendable value increases in line with AUM growth, the EMEA region is declining in lendable value, despite the growth of inflows. There has also been growth in non-cash collateral being posted for ETFs in the US recently, and utilisation in the EMEA is below 5 percent compared to 20 percent in the US. Why are ETFs growing in Europe but their use as collateral in securities lending is not?

A Securities Lending Times and Markit survey of 66 professionals who work in securities lending in some capacity revealed that liquidity is the most important consideration to them when deciding what to accept or post as collateral, outpacing cost and risk weighting by some margin. When they were asked whether they accept or post ETFs as collateral, the majority of respondents who are located in Europe were split, with slightly more saying they accept or post ETFs as collateral than those who said they do not. The response from those located in North America was equally close.

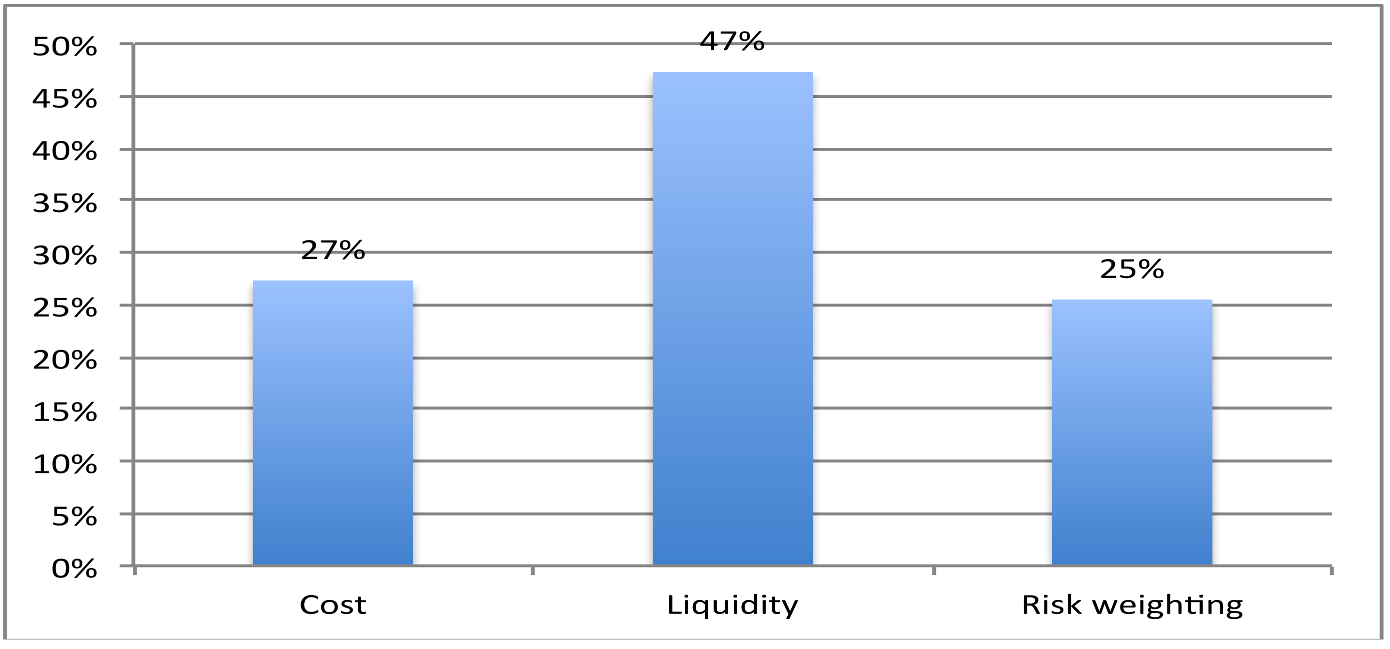
Today, less than 5 percent of ETFs in Europe are used for lending compared with an estimated 25 to 30 percent in the US, says Andrew Howieson, a securities lending consultant and author, but that will change as the trend towards passive index investing continues to develop and ETFs win greater favour in the asset allocation process.

Andrew Jamieson, global head of broker-dealer and market-maker relationships at BlackRock, is seeing these very trends in action. He says: "It is almost a classic virtuous circle we are witnessing. As products become larger and more liquid, this pulls in more institutions, attracted by the liquidity. People are using the product [ETFs] more and more."

Jamieson identifies a number of tailwinds driving ETF growth, especially when compared with other forms of structured products. "As regulations change, products such as over-the-counter (OTC) derivatives become ever more expensive. Because ETFs are larger, costs are lower and this benefit is passed on to investors."

Growth in the adoption of ETFs will continue if fixed income investors increase their participation, says Jamieson, as the move towards passive index investing gains pace. ETFs provide a natural way to take a view on

What is the most important consideration to you when making a decision about what to post or accept as collateral?



fixed income and they offer greater liquidity than the usual alternatives. Fixed income investors in particular need to go long or short, and the ability to borrow ETFs is becoming essential.

These investors are in luck, because ETF liquidity is as robust as ever. According to recent data from the London Stock Exchange (LSE), there are currently more than 1,200 ETFs and ETPs listed on its main exchange, and the total value of ETFs traded on-exchange this year has reached £175.7 billion, notes Source ETFs, one of Europe's leading ETP providers.

Most of the European investment in ETFs comes from institutional investors, but Source is forecasting that there will be a significant increase in demand from retail investors, primarily through their advisors. Over the past 12 months, nearly one in five financial advisors said their clients have increased their exposure to ETFs, as opposed to just 3 percent who have seen clients reduce it.

Over the next year, one in three independent financial advisors expect clients to increase their exposure to these investment products compared to 4 percent who anticipate exposure will fall. Some 59 percent of independent financial advisors said that lower charges give ETFs an advantage over other investment funds, followed by 21 percent who said it was about innovation, and 13 percent who cited the wide choice of ETFs available.

Source is already capitalising on this market growth. It has attracted $3.4 billion of assets so far this year (as of 15 September 2015), which is equivalent to 20 percent of the firm's AUM at the beginning of 2015. Just over half of this, $1.8 billion, has been into fixed income ETFs, with $1.3 billion into equity ETFs and $300 million into commodity products.

Gillian Walmsley, head of fixed income and listed products at the LSE, said on 22 September: "London has long been seen as the capital of the ETF industry in Europe, with deep liquidity and a strong emphasis on promoting transparency. In 2015, 101 new ETFs and 25 new ETPs listed on the LSE. Total on-exchange value traded for ETFs this year is up 61 percent compared to the same period last year."

Lee Kranefuss, chairman of Source, added: "Our research shows that the UK and European market has huge potential for further growth. In a poll of more than 100 independent financial advisors in the UK, 14 percent of them said they do not fully understand ETFs, and 34 percent said that their clients do not fully understand them."

The potential for retail investors is particularly intriguing. Jamieson says ETFs have the potential to democratise institutional investment practices, enabling retail investors to access the world of short and long performance.

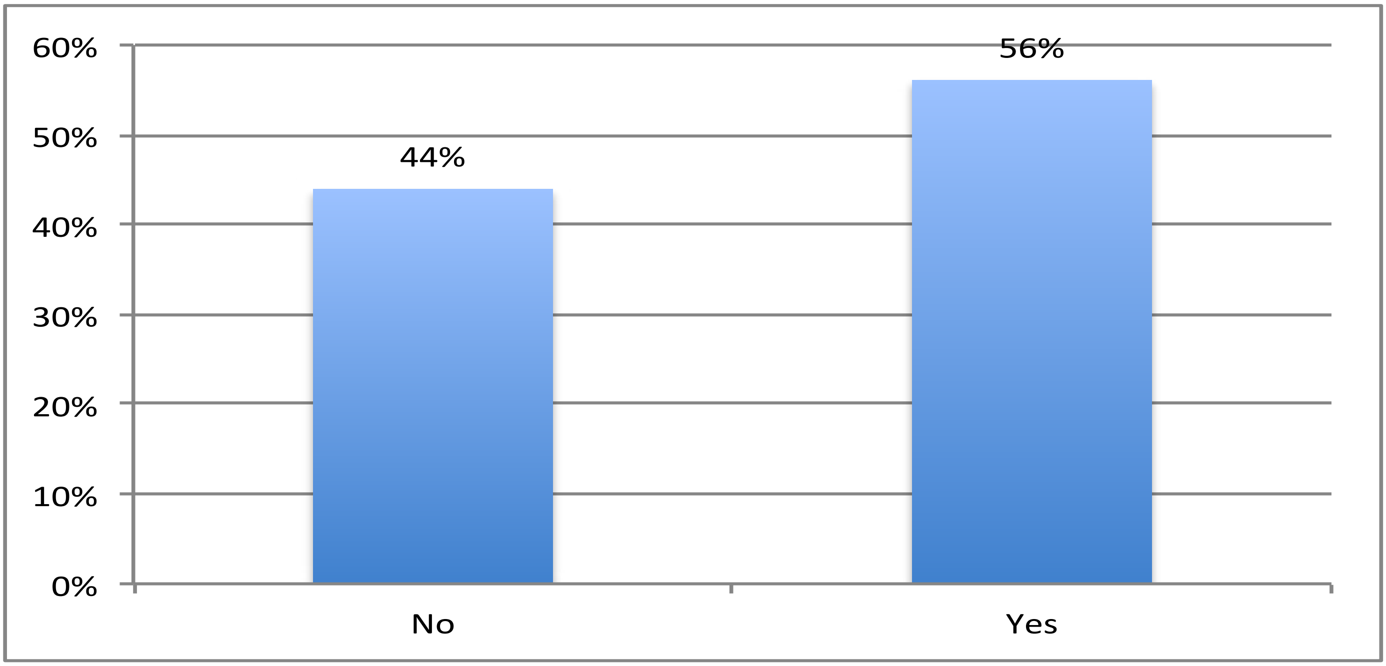
Jamieson explains: "Retail investors couldn't previously dream of being able to profit from an asset they have never owned. ETFs will allow them to do that. They [ETFs] are a unique phenomenon, a technology, a wrapper, rather than an asset class, which could become the biggest component of price discovery ever known in our industry. Securities lending is essential for the increased growth and greater operational efficiency in any market."

ETFs appear to represent a ripe opportunity in European securities lending. Although barriers to their use do exist, efforts are being made to overcome them.

Mo M'Rabti, deputy global head international markets at Euroclear, says that post-trade processing, reducing costs and boosting liquidity are among the areas that need work before the uptake of ETFs as collateral in Europe can improve.

He says: "Borrowers have shown some appetite for borrowing ETFs, but the traditional model of issuing in different domestic markets with different codes and settlement procedures has meant the available pools of capital have been locked into silos, and fees have been high. Why pay 200 basis points for an ETF when you can borrow the underlying securities for 30 to 40 basis points?"

Do you post or accept ETFs as collateral?



This helps to explain the discrepancy between the lending and borrowing of ETFs in the US single market and Europe's fragmented markets—moving ETFs across borders is complex, costly, takes time and is not without operational risks. The centralisation of securities will help to redress the balance, says M'Rabti, as settlement in a single centre is evidently better than settlement in multiple places. "This is why issuers are pushing us to centralise post-trade processing in order to create a real single market for ETF securities in Europe. The market told us that post-trade plumbing was a real concern and we have addressed that."

Euroclear is seeing a growing number of ETFs on its centralised international platform, which concentrates the settlement of ETFs in its international central securities depository (ICSD), paving the way for lenders and borrowers to interact more easily. BlackRock is issuing all new European ETFs via the platform and plans to migrate all of its existing ETFs over the next 12 to 18 months on a staged basis.

"Post-financial crisis, the ETF has been a success," says M'Rabti. "Our pipeline of new issues is healthy and I am very optimistic. We have worked hard with the industry to get lenders contributing to a bigger centralised pool and to educate borrowers to the enhanced availability that our efforts have delivered. Having everything in one place will improve the prospects for securities lending involving ETFs. Lending boosts liquidity, which in turn boosts a market's reputation."

He adds: "ETFs, a booming asset class, have traditionally been prone to failed settlement; lending should help that and they could also be used as collateral and for securities financing, enabling the development of longer-term lending as is commonplace in the US. The potential is there and growth will accelerate within the ICSD model. Of that we are certain. We are seeing activity on our books and the model is working efficiently across multiple currencies and across all time zones."

Richard Glen, head of global securities financing sales and broker-dealer relations in the UK and Ireland at Clearstream Banking, says: "In the changing world of collateral management, traditional counterparties have to make their balance sheets sweat more than ever. We have invested heavily in allowing clients to use a broad range of funds from mutual funds to ETFs as collateral."

"As equities and ETFs are very much in vogue today, we spend a lot of time talking to clients to ascertain their requirements and with our links into multiple CSDs we can settle ETFs across our books in a similar way to equities."

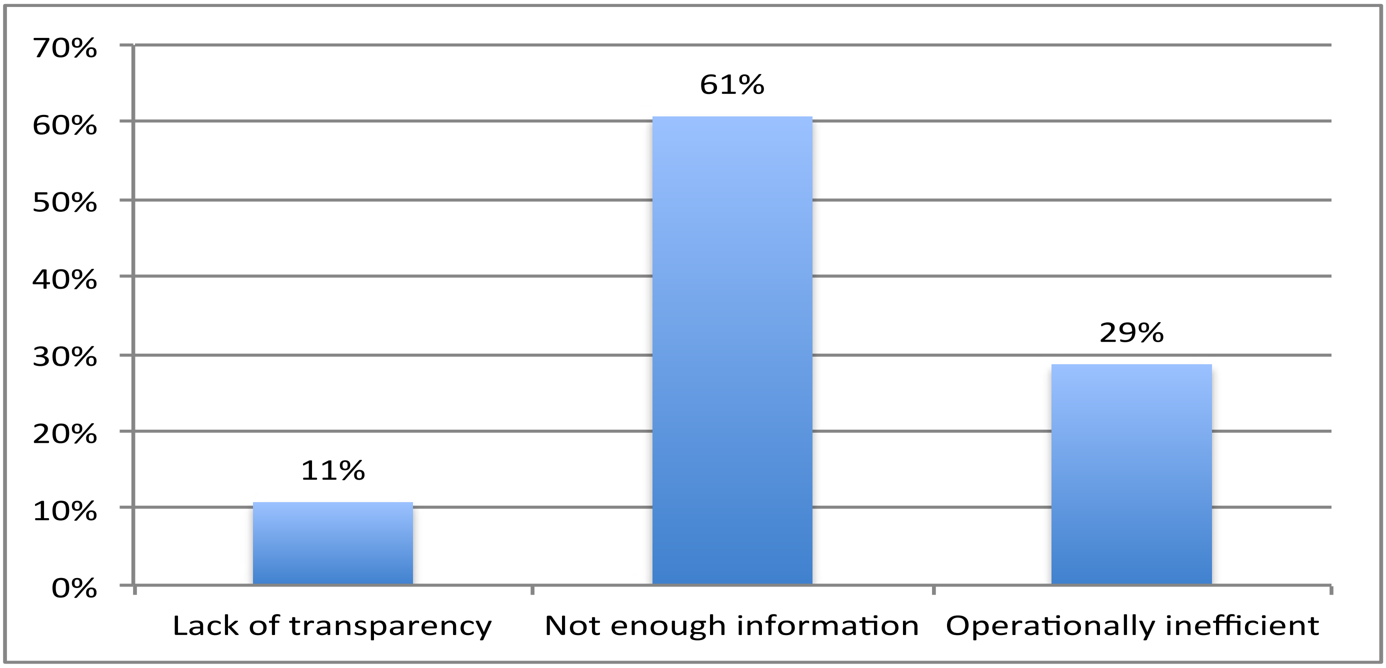
The European respondents to the Securities Lending Times and Markit survey who do not post or accept ETFs as collateral said they largely do so because there is not enough information available. Interestingly, one agent lender said there is a lack of demand for ETFs as collateral in securities lending, while a broker-dealer said they are usually not accepted, suggesting that beneficial owners are not confident in their knowledge or understanding of ETFs.

Mark Schaedel, managing director in the information division at Markit, which among other services assists ETF issuers with the mechanics involved in a new listing, stresses the need for cooperation and collaboration to improve knowledge and understanding. "We need to maximise the use of ETFs as a community. Everyone in that community has a common interest in seeing ETFs grow. ETFs, however, suffer from a lack of transparency, which is almost as big a hindrance to further development as the perceived lack of liquidity."

Respondents to the Securities Lending Times and Markit survey offered a resounding view of what they believe to be the most inefficient aspect associated with posting or accepting ETFs as collateral. Some 60 percent said ETFs have too complex a risk profile and suffer from the lack of any standard identification process.

An increase in market transparency will need to be achieved to underscore the differences between individual ETFs. One of the most obvious is whether an ETF is physically backed by the purchase of the underlying paper or commodity, or whether it is synthetically backed.

Why do you not post or accept ETFs as collateral?



With physical backing, investors can touch the ring-fenced asset and not have third-party exposure.

Physical backing features in the approach that Markit has taken in doing to help drive the industry towards using ETFs as collateral by creating a number of standard ETF collateral lists. It draws inspiration from the paper authored by Roy Zimmerhansl and Andrew Howieson in 2012. This paper noted the lack of a comprehensive industry classification system and the inability to group ETPs based on certain criteria. Solving these problems would alleviate the need to deal with ETPs on an ISIN by ISIN basis. Pre-defined lists that follow risk department requirements would enable the grouping of ETPs onto a broader multi-asset collateral schedule.

Markit is well positioned to facilitate the classification and grouping of ETPs as it has been providing data services in the ETP and securities finance landscape for more than 10 years. "We want to highlight ETFs' potential, using existing infrastructure," says Schaedel. "We could see massive growth in the market once we work out how to use them better and introduce them to the retail investment mainstream."

A sustained education programme will be required, teaching investors how to understand ETFs and how to use them, as well as about their qualities as an asset that can be lent and borrowed, he indicates. This would address, in particular, the perceived lack of liquidity referred to in almost any conversation on the topic. This, Schaedel attests, is illusory. "ETFs are of the same quality as the underlying assets. Why wouldn't you accept a fund comprising shares if you would accept the shares themselves?"

The answer to that question is, he says, in the additional work needed to assess whether an asset class passes risk acceptability criteria, which is work done at fund level rather than at index level.

Schaedel explains: "If an asset is FTSE 100, it is acceptable, but not ETFs, where the risks are just not what they are perceived to be. With this in mind, we are trying to recreate workflow convenience for an ETF as we see for indices, to produce a list of ETFs that are very transparent for equities and fixed income."

After a consultation period, Markit announced in August this year that it would publish two inaugural ETF collateral lists, for physical equity and physical fixed income. Markit's ETF collateral lists would be based on key filtering criteria such as replication methodology of the ETF, country and index exposure, as well as tracking difference.

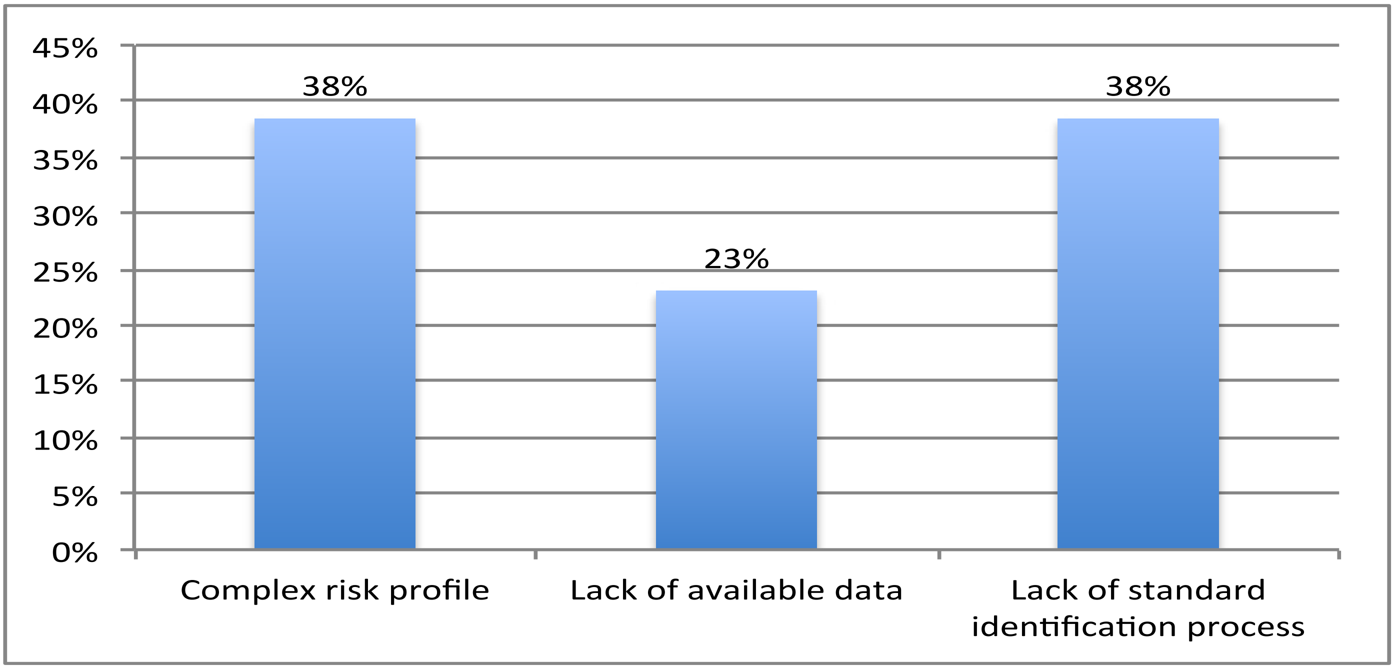
In the initial lists, an ETF will need to be physically replicated, which ensures that the collateral taker, when redeeming the ETF, will receive the underlying assets in the approximate weights of the underlying index and can benefit from the multiple disposal options. The filtering process provides assurance that the ETFs have met the approved criteria.

As market participants become comfortable with Markit's standard ETF collateral lists, there will be opportunities to expand the filtering criteria to include other asset classes, indices, synthetic ETFs and more. This initiative should have positive effects on all aspects of utilising ETFs in Europe and will support their growth.

The ability for lenders and borrowers to agree on a group of ETFs as opposed to tackling the task on a case-by-case basis should bring much needed efficiency to the market, Markit notes in its whitepaper, The Case for ETPs as Collateral. "If we succeed in exposing ETFs to the securities lending market, it will be easier to trade ETFs and for hedge funds to take positions using them," concludes Schaedel.

The rise of the ETF is as clear as the path towards their use as collateral in securities lending. ETFs are becoming more liquid as institutional and retail investors learn about their benefits. As that happens, they become more appealing to securities lenders and borrowers looking for transactions that strengthen the risk versus reward calculation in their favour. ETFs are here—and the work is well underway to ensure they stay that way.

What is the most inefficient aspect associated with posting or accepting ETFs as collateral?



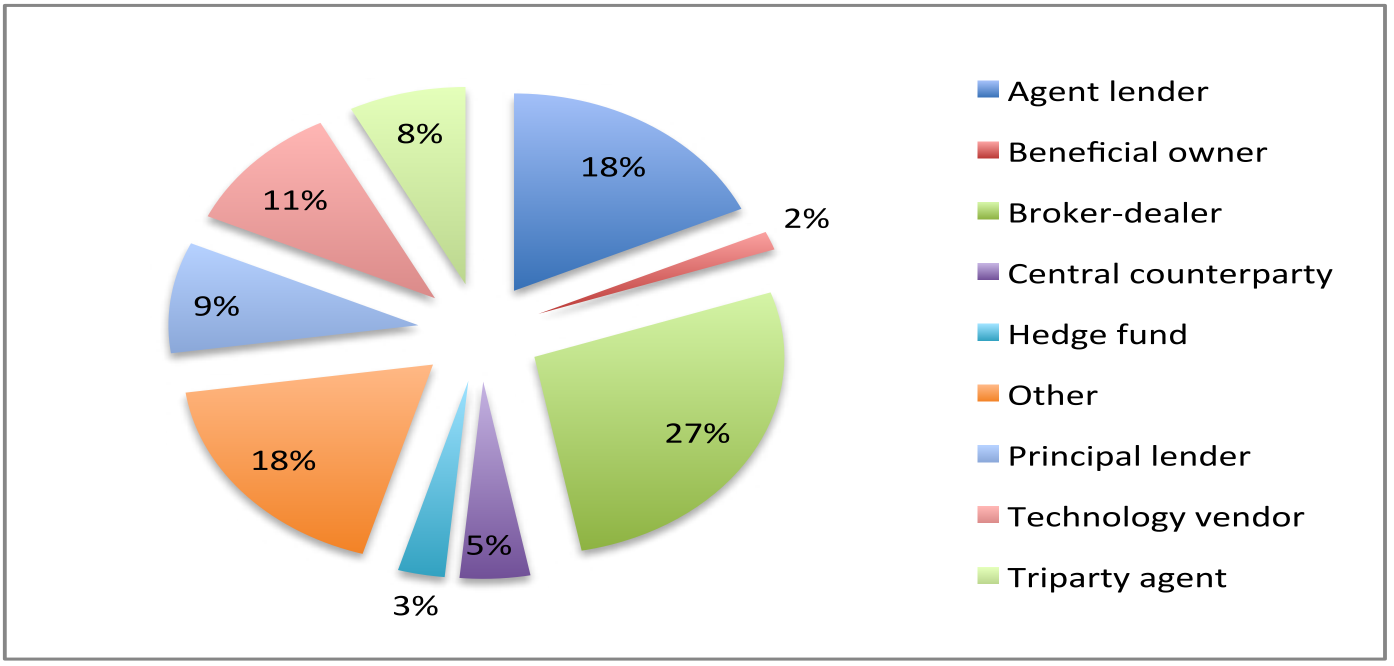
SLT and Markit survey

Securities Lending Times and Markit conducted a survey of securities lending professionals to find out why ETFs are not widely used as collateral in Europe and what can be done to make them more acceptable to borrowers and lenders.

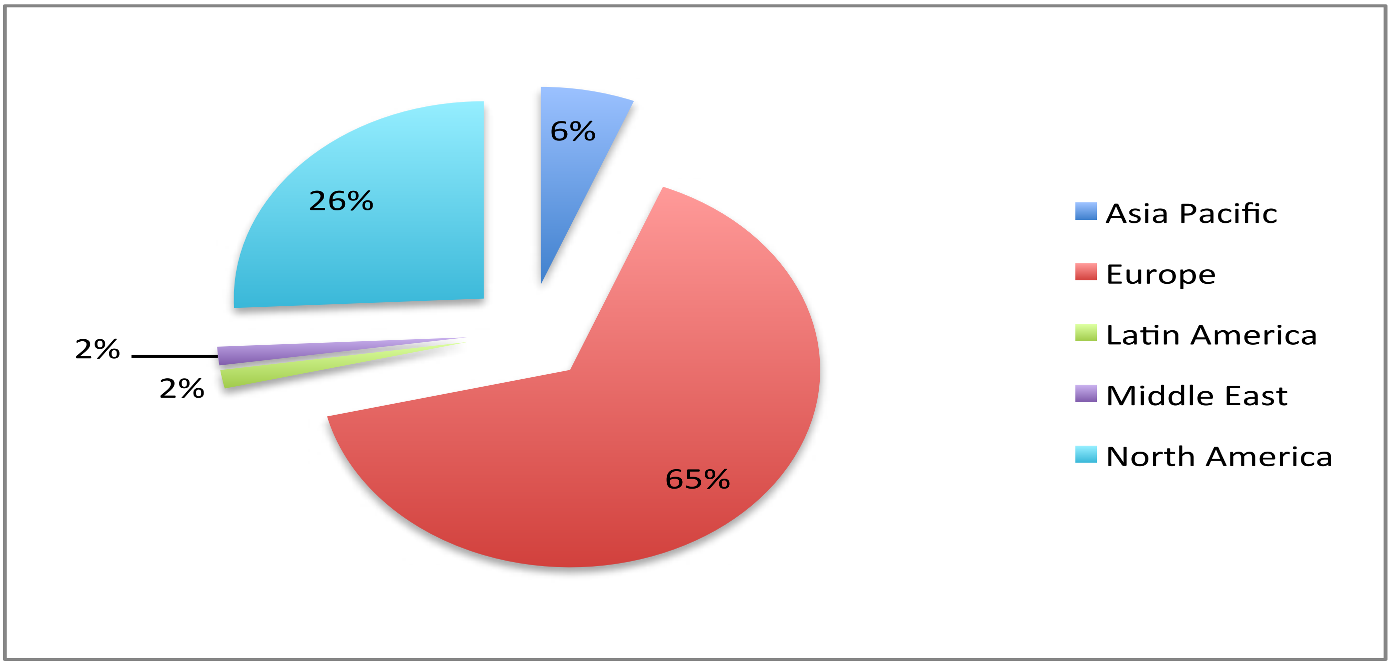
The survey was carried out online in August and September and attracted responses from across the industry, including investors, broker-dealers, lenders, triparty agents, heads of delta one sales, traders, hedge funds, central counterparties, capital markets managers and technology providers. The respondents predominantly hailed from Europe. The rest were located in North America, Latin America, the Asia Pacific and the Middle East.

The quantitative data was then supplemented qualitatively by a series of targeted conversations with senior industry players.

Industry respondents by business



Industry respondents by location



It's quiet—almost too quiet

The regulatory overhaul of securities lending and the possible role of central counterparties dominated this year's RMA conference in Miami

DREW NICOL REPORTS

Those hoping that a regime change in the US after the presidential election will save their business from the oppression of Basel III are out of luck, heard attendees at the 32nd Risk Management Association (RMA) Securities Lending Conference in Miami.

Gregory Lyons, partner at Debevoise & Plimpton, explained that the current terms of Basel III are here to stay, as they're implemented through regulatory, not legislative action.

The first session of the conference analysed the current regulatory landscape and looked back at how far the securities lending industry has come since the RMA conference last year.

"It's been a relatively quiet summer, too quiet some might say," said Lyons.

Q4 2015 and Q1 2016 will likely revive the tempo of industry change as all major regulatory bodies are expected to make major announcements concerning their vision for the next 18 months at the G20 summit, which begins on 15 November.

"It's going to be a busy Christmas and New Years for all of us," added Lyons.

The US Securities and Exchange Commission, the Basel Committee, the Financial Stability Board and the International Swaps and Derivatives Association (ISDA) are all expected to use the occasion to deliver further details on issues such as the so-called 'Basel IV' initiative, the ISDA stay protocol and total-loss absorption capacity.

'Basel IV' is the unofficial title given to plans to tackle the variables that currently exist in the way different states in Europe and the US interpret some aspects of regulation. The aim is to close any potential loopholes that allow international companies to exploit the rules to get better treatment by the regulator by shifting assets to different regions.

After outlining the numerous regulatory hurdles being tackled presently or on the horizon, the point was raised that with all the new regulatory proposals being put forward, very little time had been given to reviewing how all these new restrictions would work in tandem, and their combined impact on the market.

With the development phase of most of these new rules now complete, there's a need to do just that as it recently emerged that European repo activity had dropped significantly in 2015 and is stagnating under the weight of the new regulations.

The Bank of England, as one panellist pointed out, has since commissioned a study into whether the financial markets, although technically more stable, are actually being crippled by the new framework and whether a compromise needs to be reached.

Although this will be positive news for many, another panellist quickly reminded the audience that "US regulators disagree entirely and are showing no sign of slowing down on their efforts".

All conversations of regulation ultimately led back to Basel III as the panel gave an update on the progress of the implementation of the liquidity coverage ratio and the net stable funding ratio (NSFR). The panel aligned itself with the majority of the industry's belief when it was prediction that the NSFR, although not due to go live until 2018, would become a regular feature of the industry much sooner as the market would force banks to adopt the ratio as best practice long before the due date.

Another conference speaker turned to the burden of multiple variables in risk weighted assets calculations across different markets.

This trend can be clearly seen, explained the speaker, by the way European and Asian markets, which have much wider variables between independent countries than between states in the US, are much further along this path, although admittedly, there are other constraints on the US that are also slowing this shift.

The conversation then shifted to the ongoing and emotive subject of central counterparties (CCP) and their place in the world of securities lending.

With no CCPs on the panels, the debate was primarily from the agent lender and broker-dealer perspectives and most agreed that there was a place for CCPs as a 'tool in the toolbox', but too many questions marks remained to make concrete predictions for the future.

Agent lenders will become clearer about their inability, or unwillingness, to indemnify all trades. Whether this will increase the attractiveness of CCPs as an alternative risk mitigation tool remains to be seen, heard conference attendees.

The second day of the conference opened with a rigorous analysis of how the bond market will cope in the event of an interest rate hike.

"The thing that is on everyone's mind is what will happen when the Federal Reserve starts tightening [interest rates]," commented one panellist.

"There will always be liquidity, it will just be at a greater price", responded another. CCPs were recommended as a solution to how direct repo transactions could operate as another source of liquidity.

"In the current world we live in, a CCP is the solution," observed a speaker. "But to get it right it needs to be all encompassing."

Another panellist agreed and suggested that it would be crucial for any CCP solution to tackle the problems that were at the core of the 2008 crash.

In the second panel, attendees learned that agent lenders have had to adapt to a world with less collateral available and less flexibility in dictating what their clients post. This has led to a shift away from high-quality liquid assets (HQLA) towards accepting equity as collateral.

The point was made that not all beneficial owners are equal, and neither are all borrowers. Beneficial owners are becoming increasingly picky about their collateral parameters and causing headaches for their agent lenders, which are struggling to marry up lenders and borrowers with similar strategies.

The majority of the panel, made up of agent lenders and broker-dealers, agreed that the securities and correct collateral did exist in the market, but "mobilising" it with all the restrictions

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in place is one of the biggest challenges they face day-to-day.

The agent lending disclosure (ALD) went under the microscope in a roundtable on market transparency.

A work group has been set up to create a two-way dialogue between regulators and the industry to improve the quality of reporting data from the market.

A pilot reporting programmee has since been created by the US Treasury and templates have been sent to select participants to test the new minimum standards for reporting. The aim is to tackle issues around the inconstancies and inefficiencies in the current data being reported to regulators.

The ALD work group will submit a new set of minimum standards that individual states can then choose to build upon or maintain.

Although the project is moving forward, some concerns have been raised that most financial institutions don't have the technology to provide the level or format of data being requested.

The US focused work group is engaging with members of the European Central Bank to try and minimise the reporting burden for international firms that will have to report data in separate styles to each of the relevant regulators.

"ALD groups are going to be very busy over the next two years," predicted one panellist.

Harold Ford Jr, five time Democrat congressmen for Tennessee, was the keynote speaker for this year's conference. He gave a knowledgeable overview of the US political landscape in the lead up to next year's election.

Ford also offered his perspective of dealing with the wider financial markets from the point of view of the government itself.

In keeping with the theme of shifting perspectives the next panel looked at the very topical issue of China and the Asian securities lending markets.

A summary offered by one panellist highlighted that the summer's market turmoil had caused a decrease in borrowing and that there was a serious lack of appropriate collateral.

When discussing the impact of the Shanghai-Hong Kong Stock Connect on the securities lending industry, one speaker commented: "It will take years before we see more activity and it will take a long time for investors to get comfortable with the product."

"There's education that needs to be done and it will take time."

Another speaker replied: "I'm bullish in terms of the future."

As China begins to open itself up to outside investors, some concerns were raised about how the influence of Hong Kong, as the gateway to China, will be affected.

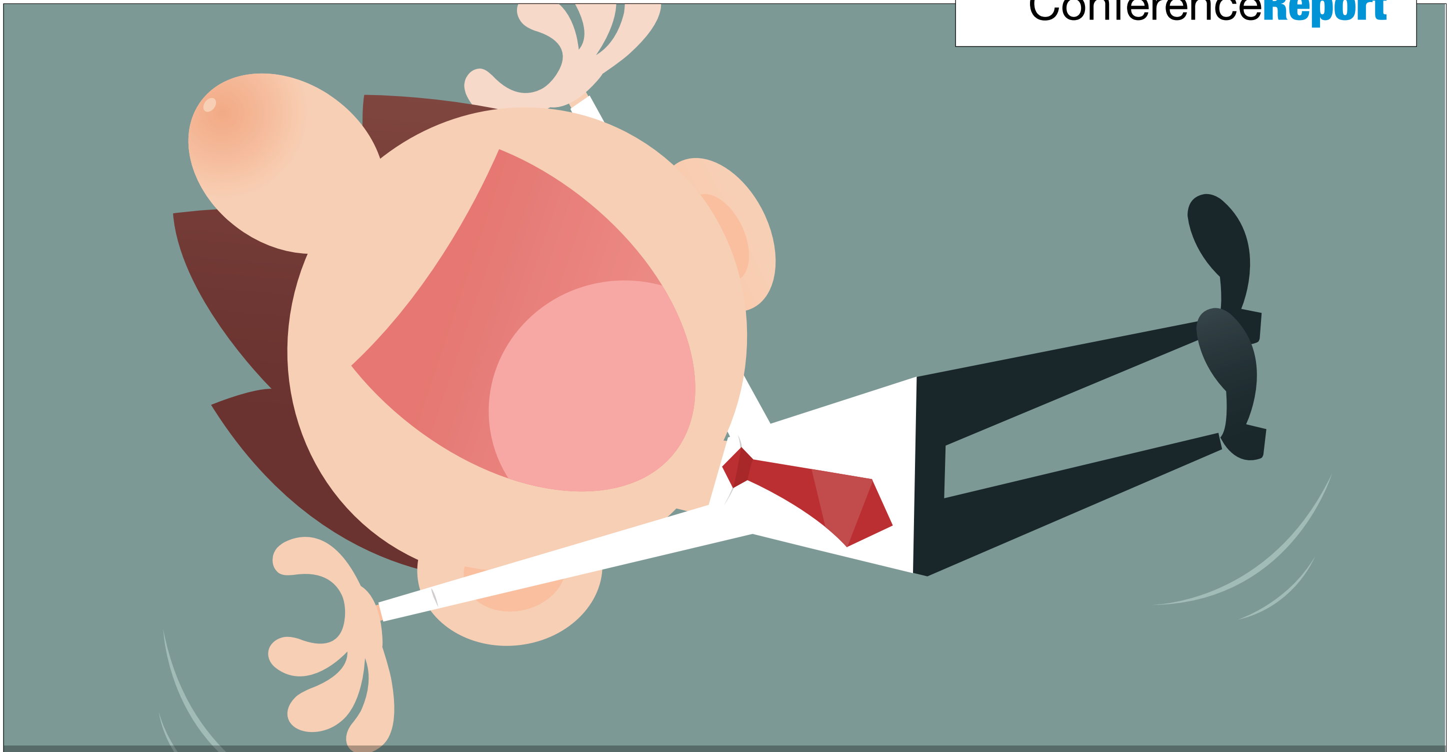
As one panelist put it: "The problem is there is no benefit currently with regard to Hong Kong for securities lending and borrowing, or the Stock Connect, because the assets are not held with the participants."

The final panel of the event included leaders from across the industry who gave their analysis of the past year and looked forward to what the major talking points would be in the future.

"Securities financing is essential for the functionality of all the other markets around our industry," argued Thomas Wipf, managing director at Morgan Stanley.

Overall, it was agreed that 2015 had been a good year for the securities lending industry and with many of the final details of the new regulations becoming clearer, industry players are able to get on with the job of implementation and expanding their businesses.

"People are more positive this year," commented one industry leader. "Last year people were still creating their strategy but this year people know what they're doing." SLT



The silo is dead, all hail pooling!

Fleming Europe's Annual Collateral Management Conference saw a variety of industry figures come together to debate the best way to manage and leverage collateral in an increasingly strict regulatory environment

DREW NICOL REPORTS

Repo is dying, centralisation is the key to optimising collateral management, the shift from cash to equity is all but complete in some trade types—these were just some of the claims made during this year's Collateral Management Conference.

The conference, now in its ninth year, proved to be the largest one so far, with almost 200 industry figures descending on the iconic city of Amsterdam for the two-day event.

The mandate of the conference was a simple one: to analyse and discuss the various regulatory, economic and operational challenges market participants face when managing collateral effectively.

Collateral held by banks and asset managers can be utilised for a variety of purposes if managed correctly. These include securities lending, liquidity management through repo activity and meeting regulatory requirements, such as the liquidity coverage ratio (LCR) and net stable funding ratio (NSFR), under Basel III.

As more and more of the new regulations reach implementation, the importance of optimising collateral to meet new guidelines will only increase and affect market participants right across the spectrum of industries.

It is therefore unsurprising that the conference was attended by a wide variety of financial industry players, from central counterparties (CCPs) and other service providers to investment banks and technological solution suppliers, with representatives from all over Europe and beyond making the trip.

Decisions, decisions

The conference kicked off with an in-depth look at the many regulatory considerations in an environment of rising volumes of collateral, increasing margin calls and more and more counterparties looking to wedge themselves between the buy and sell sides.

"Europe culturally doesn't make it easy on itself", lamented one panellist during an early discussion on how the US and the EU compared in efficiency when creating new regulation. "The regulatory tsunami is coming," replied another.

The very nature of Europe as a collection of individual markets, of varying levels of development, is the main stumbling block to any new regulation and the reason why Europe's answer to the US Dodd-Frank Act is so slow to materialise, according to a third speaker.

Part of the dreaded regulatory tsunami is the European Market Infrastructure Regulation (EMIR), which polled as the regulation causing the most concern for audience members.

And indeed the first 'controversy' of the day came when a panel discussion on the collateral segregation models options under EMIR concluded that the basic omnibus model, where positions and collateral are co-mingled, was by far the most popular choice, only for the audience poll to reveal 70 percent planned on utilising the more extravagant 'full segregation' model. The omnibus option only earned 11 percent.

Andrea More of BNY Mellon offered a reasoning to the disparity, stating: "People want full segregation but the actual cost is much more than most people can pay."

The full segregation model has a "Porsche effect", explained More. Market participants initially like the idea of having the best and flashiest model, until the reality of the price tag versus their actual budgets hits home.

The issue of conflict in the most appropriate segregation model resurfaced during a roundtable featuring CME Clearing's Dennis Mullany and Eurex Clearing's Philip Simons.

"It's very regionally and client specific," commented Simons while explaining why no clear conclusion could be reached.

Mullany said: "We've been taking this survey for four years and we still see [the] full segregation model coming to the fore."

After a fourth year of debate, a poll still showed that roughly half of those in attendance didn't have (or weren't aware of) their firm having a clear strategy with regard to segregation models, but everyone could agree that managing costs was the primary driver behind all decisions on future investments.

Bridging the gap and making time

The increase of margin call volumes and the impact of new margin requirements for non-cleared derivatives took centre stage in the afternoon. The burden on operations and infrastructure from regulation and building costs was outlined by one speaker.

Cash is still king when it comes to variable margins', was the clear message of the session, along with the fact that securities lending and repo are legitimate and effective ways of financing collateral in the short to medium term.

Despite all of the progress made in combatting new and increasing costs in managing liquidity and risk, there is still a lot more work to do. "It's not time to relax, the biggest challenges are still ahead," concluded David Béatrix of BNP Paribas Securities Services.

The advantages of pooling of collateral from all the different trading desks was advocated by multiple speakers throughout the event. It was argued that pooling collateral into one platform allows collateral managers to survey and allocate their collateral inventory much more effectively. It also offers a clearer picture of the total costs and reinvestment options open to them.

"You have to move away from the silo approach and start to pool all your collateral together," explained one speaker. "Understanding your costs better leads to a much better management of inventory."

This view was echoed by Ted Allen of SunGard in his presentation on why collateral management should be "partly" viewed as a front-office function.

"Centralisation [of collateral] is key," he commented. Investing in a central collateral and liquidity management and trading unit, which would include repo/reverse repo and securities lending activity, along with all available collateral, would help "unlock the potential of collateral management".

Other than emphasising the need for a pooled approach, Allen's talk focused on collateral transfer pricing and best practice for asset managers and banks.

Collateral transfer pricing (CTP) is the mechanism by which an internal market for assets is created within the institution. It ensures that asset usage to support trading activity through the allocation of capital and collateral is correctly charged, according to a SunGard report.

CTP incentivises asset holders in the firm to provide those assets to a central inventory pool for efficient allocation against collateral and capital requirements. CTP is key in the mechanism to allocate costs of collateral consumption to the underlying trading activity. This ensures correct deal pricing and profitability analysis

But, according to Allen: "There is no standardised market approach to collateral transfer pricing." **SLT**

Market volatility boosts securities lending industry

The North American market's recent slump has seen short sellers return to the market in levels not seen in several years. Markit's Simon Colvin reports

American short sellers have returned to the market after years of bull market hibernation. Average short interest in the S&P 500 index has passed the 3 percent mark for the first time in over three years, which is more than 50 percent higher than the levels seen a year ago.

This increased desire to sell shares short means that the aggregate value of all short positions, as tracked by securities lending volumes, has surged from the $500 billion mark seen at the start of the year to $594 billion as of the latest count. This surge puts the value of all short positions in North America at its highest level since 2008, when short positions were worth more than $700 billion.

The anaemic demand to sell shares short over the last few years is also represented by securities lending programmme utilisation, or the proportion of inventories out on loan at any given time. That metric has flat lined in the 5.5 to 6 percent range over the last two years of tepid shorting activity. The recent surge in borrowing activity, combined with the fact that market volatility has seen the value of assets in lending programs fall by 7 percent from the highs, has led utilisation to jump past the 7 percent mark for the first time in more than three years.

Fees hold up

While the fees commanded by lenders for North American equities to keep a short position open has not seen the multi-year highs seen in other borrow metrics, the recent weighted average of 60 to 70 basis points required to borrow North American assets over the recent period of volatility is above the 58 basis point average of the last five years.

This has helped the industry post some of its healthiest revenues in years as lenders have been able to get 6 basis points of annualised total returns for North American assets over the last two weeks, the longest such streak since the 'taper tantrum' volatility in 2013.

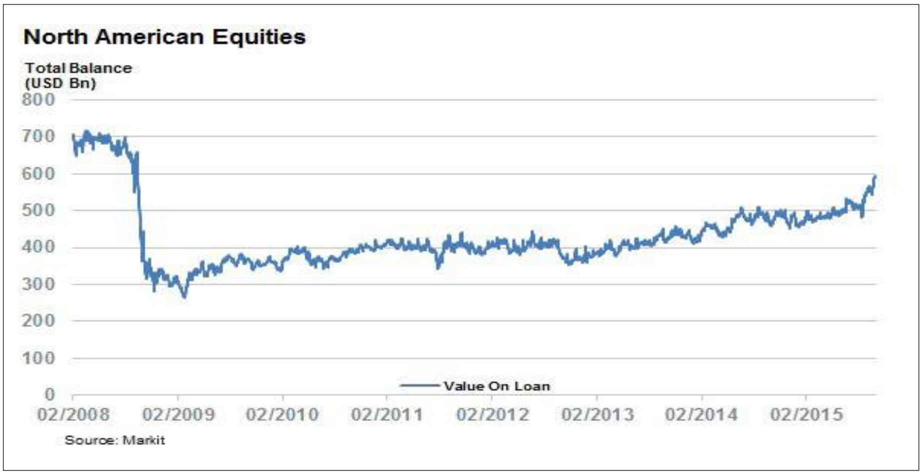
In dollar terms, the revenues generated by North American assets since the start of October are up by 18 percent from the same period last year. While it's still very early days for the fourth quarter, should the trend hold up, we could see the best quarter for the industry in revenue terms since the financial crisis.

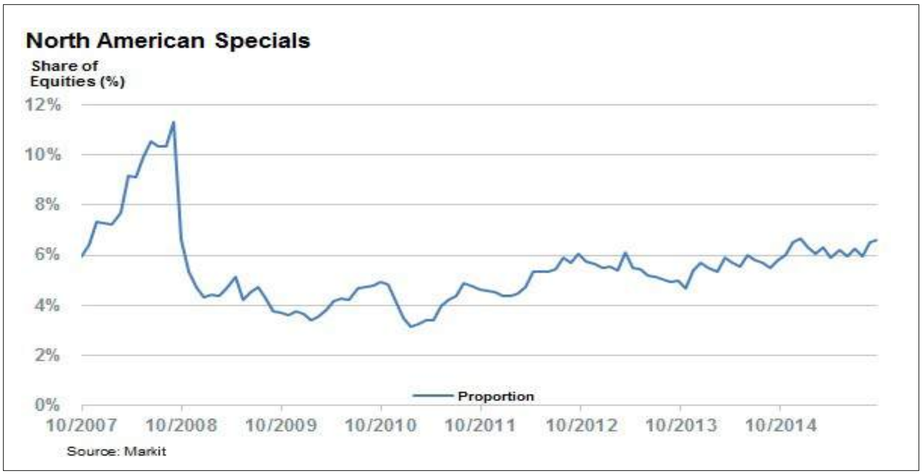
Specials jump

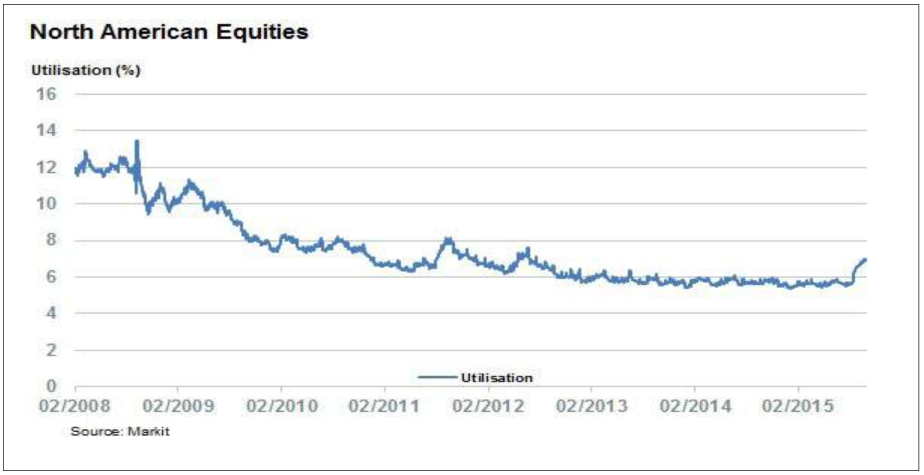
A large part of the revenue story will be driven by the proportion of shares trading 'special'. The proportion of shares that command a fee of more than 100 basis points a year to borrow now stands at 6.6 percent of shares, the highest proportion since the financial crisis. Not surprisingly, energy names have been the shares which short sellers are the most willing to pay up for.

There are now 43 energy names trading special—50 percent more than at the start of the year.

The other sector to see a large jump in specials is materials, which has seen its number of specials surge. **SLT**







Industry appointments

BMO Global Asset Management has confirmed its recruitment of **Christopher Kunkle** as managing director of securities lending.

Kunkle's new job, which was exclusively revealed in August, will see him take overall responsibility for managing, developing and executing the firm's securities lending strategy.

He will also oversee third-party agency sales and distribution, relationship management, product development and operations, as well as legal and regulatory issues.

Kunkle was previously managing director of client transaction services and securities finance at Wells Fargo. Before that, he served as the Risk Management Association's director of securities lending and market risk.

Steve Arquilla, COO of BMO Global Asset Management in the US, said: "Chris Kunkle is an experienced leader with an extensive knowledge of the securities lending industry that will be a valuable asset to our team."

"I'm confident he will continue BMO's track record of success in both developing approaches tailored to our clients' needs and looking beyond lending to help our clients understand the changing regulatory environment."

Weeden Prime Services has hired **Will Greco** as head of capital introductions.

The team's expansion is in response to a period of strong growth resulting from the recent tumult in the brokerage industry caused by J.P. Morgan's decision to exit the correspondent clearing business, according to Weeden Prime.

Greco brings more than 15 years of experience in the prime brokerage and capital introduction space.

Most recently, he was an a central player in the capital introductions team at Jefferies, and also served in similar roles at Lazard Capital Markets, Bank of America and BNP Paribas.

"Capital introduction offers most prime brokers an opportunity to distinguish their offering, however, most prime brokers have an impossible task of delivering truly customised service to their clients," said Greco.

"I am excited to be a part of a growing business that is in a great position to offer clients a dedicated platform to help grow their businesses."

The chief executive of the Investment Association has stepped down from his role with immediate effect.

Daniel Godfrey was appointed to the role in December 2012.

The Investment Association, whose UK investment manager members collectively manage more than £5.5 trillion in assets, has named **Guy Sears**, currently director of risk, compliance and legal, will take over on an interim basis until a permanent replacement for Godfrey is appointed.

Helena Morrissey, chair of the Investment Association, commented: "The board would like to thank Godfrey for his significant contribution to the Investment Association."

She added: "During his time Godfrey has driven a number of important initiatives, including the transformative merger with ABI Investment Affairs."

"His commitment and passion for our industry is widely admired by all those who have worked with him. We owe him a great debt of gratitude and wish him the very best for the future."

CloudMargin has recruited **Karl Wyborn** as managing director and global head of sales.

Wyborn will be based in CloudMargin's London headquarters.

He will oversee all sales activity for its risk and margin management platform for the buy side. Previously, Wyborn spent 18 years at J.P. Morgan Chase, where he divided his time between London and Hong Kong as head of sales and relationship management for clearing, custody and collateral services.

Andy Davies, CEO and co-founder of CloudMargin, said: "We are hugely excited to welcome Wyborn into the CloudMargin team."

"He brings with him a wealth of experience and his extensive collateral management background makes him a very valuable addition to the company."

"I'm thrilled to be joining CloudMargin," added Wyborn. **SLT**

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