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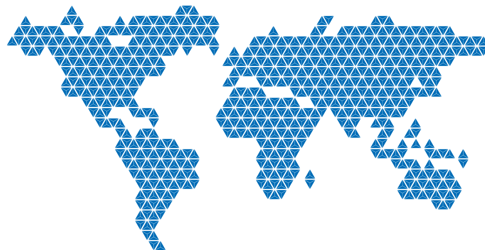

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Banque de France has launched securities lending on GC Access

France's central bank has made high-quality collateral available for securities lending through Euroclear's GC Access programme.

Euroclear's GC Access facilitates access to high-quality collateral where lenders and borrowers can access baskets of top-grade assets against other collateral in order to earn incremental value and meet regulatory liquidity requirements.

Banque de France's securities, purchased under the Public Sector Purchase Programme (PSPP), are eligible following the cash neutrality principle, at a spread over prevailing rates of between 10 to 25 basis points.

The accepted loan maturity is either one week or one month. One-week operations will not be renewed more than three times and the value date will be T+1 or T+2.

The list of PSPP securities available for lending is published every Monday on the bank's page on Bloomberg and BDFPSPP1 on Reuters.

The central bank will continue its fail prevention scheme through bilateral repo operations at T+0, provided market participants' requests are submitted before noon.

Borsa Istanbul introduces short indices

Borsa Istanbul, Turkey's primary stock exchange, will start to calculate leveraged and short indices that cover investment strategies from 1 April.

The exchange expects the leveraged and short indices to provide the opportunity to get same or inverse index exposure in return for smaller cash positions.

The objective of leveraged indices is to reflect the return of a reference index (underlying index) by a multiple of the leverage factor in the same direction.

Leverage is obtained by borrowing money and investing more in the underlying index. The borrowing cost of the leverage is supposed to be daily repo interest rates.

The index is calculated by deducting the borrowing cost (return on BIST-KYD Repo (Net) Index) from the return on the underlying index.

Short indices reflect the return of a reference index (underlying index) by a multiple of the leverage factor in the opposite direction.

A short position is obtained by borrowing equities in the underlying index, selling them short, and investing the fund generated in the repo market.

The index is equal to the sum of the return on lending (BIST-KYD Repo (Net) Index) and the return on underlying index.

Indices are calculated from the closing values of underlying index and repo index. The base date of the indices is 1 April and base values are 1,000, according to Borsa İstanbul.

Hedge funds hungry for more risk

Hedge funds are revising up their risk appetites slightly after reassurance from the US Federal Reserve on the building consumer price index, according to Lyxor's Weekly Brief.

The increase in the consumer price index has contributed to depreciate the dollar against major currencies and to fuel risk appetite.

Janet Yellen, chair of the Federal Reserve, added her voice to a chorus of dovish sentiment coming from the European Central Bank and Bank of Japan, which led Lyxor's median equity beta, based on Lyxor's sample of hedge funds, to rise to 15 percent from below 10 percent a few weeks ago.

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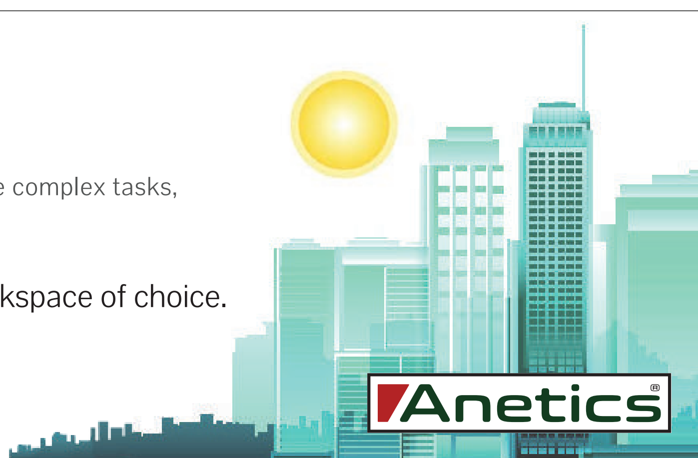

Lyxor was quick to point out that risk appetite remains well below usual levels of 30 percent, suggesting that hedge funds remain defensive and unconvinced by the sustainability of the current rally.

Emerging markets have benefitted the most, with all emerging market segments, including equities, foreign exchange and rates, rallying.

Eurex expands with US dollar futures

Eurex Exchange has launched new US dollar-denominated futures on the Euro STOXX 50 index.

The exchange, part of Deutsche Börse Group, has introduced Euro STOXX 50 quanto futures that allow investors to participate in the performance of the index without being subject to currency fluctuations between euro and US dollar.

The new quanto futures settle into the same level as the Euro STOXX 50 futures, which are the most liquid derivatives instruments in Europe, but with fees and margins being paid in US dollars.

Currently, quanto risks coming from US dollar-denominated structured products are primarily hedged by banks via over-the-counter (OTC) forwards.

Mehtap Dinc, a member of the Eurex executive board responsible for product development, said: "With the new quanto futures, Eurex will offer an on-exchange alternative to the OTC market, enabling the trading of equity/foreign exchange correlation."

"[It will] also provide non-European clients the ability to trade European equity exposure in their preferred currency."

At market launch, Eurex began offering a special market-making programme to incentivise order book liquidity.

Markit and IHS to merge

Financial research providers IHS and Markit are planning a merger valued at $13 billion.

The combined company will be rebranded as IHS Markit and headquartered in London, but with key operations remaining in Englewood, Colorado, where IHS is currently based.

IHS provides data to organisations in industries such as automotive, energy, and aerospace, defence and security.

The transaction has already been unanimously approved by the board of directors of both companies and is expected to be completed in the second half of 2016, following shareholder approval.

Markit and IHS shareholders will own approximately 43 percent and 57 percent respectively on a fully diluted basis. IHS Markit has already pledged to $2 billion of share repurchases over 2017 and 2018.

Jerra Stead, IHS chair and CEO, said: "This transformational merger brings together two information-rich companies to create a powerful provider of unique business intelligence, data and analytics to a broad and complementary customer base."

"IHS Markit and its shareholders will benefit from enhanced product innovation to deliver strong returns across economic cycles. Importantly, the two companies are values-based organisations that have a strong cultural fit which focuses on customer satisfaction and colleague success."

Lance Uggla, Markit chair and CEO, said: "This is an exciting transaction for customers, employees and shareholders of IHS and Markit. Together, we will create a global

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Uggla added: "At the heart of our shared vision is the opportunity to offer our customers a broader and richer content set through both existing and new products that will support their critical decision making and manage regulatory change. The combination will enhance cash flow and enable stronger returns of capital to shareholders."

ESMA: EU market vulnerable to high-quality collateral shortage

A bear market may cause tension in some asset market segments due to a scarcity of high-quality collateral, the European Securities and Markets Authority (ESMA) has said.

ESMA's latest Report on Trends, Risks and Vulnerabilities examines the effect that two major shifts in the European Central Bank's (ECB) monetary policy, the introduction of a negative deposit rate in June 2014 and the launch of quantitative easing in January 2015, had on the rising costs of high-quality collateral in seven EU countries over the past two years.

The analysis is based on a dataset from 7 March 2013 to 21 September 2015 and matches information on European repo markets with securities lending markets and bond-specific characteristics.

"Empirical results show that the cost of obtaining high-quality collateral, proxied by specialness of government bond repos, increases with demand in the cash market from short selling activities, even in calm financial conditions," explained the report.

"In bear market conditions—when good collateral is most needed—this may lead to tensions in some asset market segments."

"Collateral reuse may alleviate these tensions, but requires transparency and monitoring of risks from collateral chains."

The report concluded that issues raised by quantitative easing will likely be alleviated by the ECB and national central banks' securities lending programmes, which would address potential collateral shortages.

The countries used for the case study were Austria, Belgium, Finland, France, Germany, Italy and the Netherlands.

Overgrown hedge funds facing cuts

The number of hedge fund closures in 2015 was at its highest level since the financial crisis, while the number of new launches was at its lowest since 2010, according to a Hedge Fund Research (HFR) Market Microstructure Report.

Last year saw an estimated 979 hedge funds liquidated, up from 864 in 2014, representing the highest annual loss since 2009, when 1,023 funds were liquidated.

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New launches for 2015 declined to 968 from 1,040 the year before, recording the lowest total since 2010, when 935 funds were launched.

The HFR report suggests that "liquidations increased to conclude 2015, as volatility and turmoil from the second half of 2015 resulted in falling investor risk tolerance and capital redemptions from underperforming hedge funds".

In Q4 2015, 305 hedge funds closed their doors, up from the 257 liquidations in the prior quarter, and from 203 liquidations in Q4 2014.

Conversely, however, total global hedge fund capital actually grew to $2.9 trillion in Q4 2015, an increase of $22.8 billion over the prior quarter.

HFR data noted that performance-based asset gain offset a small investor net capital outflow of $1.52 billion, the first quarterly net outflow since Q4 2011.

Kenneth Heinz, president of HFR, commented: "The hedge fund industry experienced a contraction in number of funds in 2015, despite continued growth in investor capital to a record level, as investor risk aversion increased, resulting in capital redemptions from funds which had underperformed through the recent financial market volatility."

He added: "Investors have become increasingly discriminating in their capital allocations, and the environment for launching a new fund continues to be extremely competitive."

"As investor tolerance for negative performance deviations falls, and the demand for competitive fee structures increases, funds which meet these increased institutional investor requirements should attract capital and drive industry performance in 2016."

Montréal Exchange grows IRSF

Montréal Exchange is expanding its interest rate derivatives offering with the launch of Canadian dollar interest rate swap futures (IRSF), going live in September.

The new swap futures contracts will be cleared at the Canadian Derivatives Clearing Corporation (CDCC) and will be based on the Eris Methodology, owned by Eris Exchange.

The Eris Methodology replicates over-the-counter swaps economics into a single futures price, allowing the product to remain a futures contract throughout its full lifecycle, according to Eris Exchange.

Once launched, the IRSF contracts will be available for tenors of two, five and 10 years, said Montréal Exchange.

"Regulatory reforms are transforming the interest rate swap market globally, with trading markets and clearing houses taking a larger role," said Alain Miquelon, president and CEO of Montréal Exchange and group head of derivatives at TMX Group.

"By offering this innovative new product, the Montréal Exchange will provide market participants with a transparent and cost-efficient benchmark product to complement the Canadian IRS market, while also improving price discovery across the Canadian yield curve."

Neal Brady, CEO of Eris Exchange, added: "In Canada and around the world, the tightening capital constraints related to the introduction of margin on uncleared swaps, mandatory swap clearing, and revised Basel III leverage ratio calculations are driving banks and swap end users to embrace the capital efficiency of Eris swap futures."

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Securities lending ETFs barred from Taiwan currency reform

Exchange-traded funds (ETFs) involved in securities lending have been excluded from the Taiwan Stock Exchange's (TWSE) latest round of regulatory reforms of dual-currency trading mechanisms.

Taiwan's borrowers and lenders will miss out on the opportunity to branch into adding yuan certificates to ETFs, as opposed to being limited to the Taiwan dollar.

Investors can also convert an ETF from one currency to another at a one-for-one conversion ratio.

TWSE aimed to satisfy investors' demands for diversified products and asset allocation in various currencies, but deemed it necessary to exclude securities lending.

TWSE stated: "Added ETFs should be neither involved in day trades, margin transactions, borrowing of securities, and borrowing or lending money or used as collateral and underlying assets of warrants, nor subscribed or redeemed."

TWSE recently allowed brokers to borrow securities directly from customers.

Post-trade partners consider their futures and options

Broadridge and The Technancial Company (TTC) are teaming up to provide a joint post-trade offering for futures and options.

The alliance will see the combination of Broadridge's global post-trade processing solution with the strengths of TTC's real time JANUS Margin Engine.

Paul Clark, head of institutional product management, global tech and international operations at Broadridge, said: "The collaboration between Broadridge and TTC offers our mutual clients the ability to benefit from a superior, highly efficient exchange traded derivatives capability with seamless process throughput."

"The solution is integrated with post-trade processing and operational control for other asset classes offered via Broadridge's global post-trade processing platform. Our strategic alliance with TTC is a natural fit based on our shared focus to provide the highest levels of value and customer service to our clients."

Mirko Marcadella, global head of business development at TTC, commented: "Working with Broadridge enables us to provide industry participants with an opportunity to seamlessly implement a leading set of capabilities for exchange traded derivatives margin and operations."

Marcadella added: "The integrated solution offers best-of-breed post-trade processing and leverages a real-time solution developed for use from pre-trade calculations through to calculating initial margin for reconciliations and payments."

Deutsche Börse and London Stock Exchange reach merger agreement

The London Stock Exchange Group (LSEG) and Deutsche Börse have reached an agreement on the terms of an all-share merger of equals, which will not be dependent on the outcome of the UK's EU referendum.

The merger will be completed through establishing a new UK holding company, UK TopCo, which will acquire both LSEG and Deutsche Börse, governed by the City Code and the German Securities Acquisition and Takeover Act, respectively.

LSEG shareholders will own 45.6 percent of UK TopCo, with Deutsche Börse shareholders owning the remaining 54.4 percent, according to the announcement confirming the deal.

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The combined group is intended to be well placed to adapt to changes in the industry, to increase the global footprint of both organisations, and to improve reach and distribution.

The outcome of the UK's EU referendum, set for 23 June, is not a condition of the merger. LSEG and Deutsche Börse have established a referendum committee that will consider the effects of a vote for the UK to leave the EU, making recommendations to both boards, and to the board of UK TopCo, after the merger.

Both parties are of the opinion that a combined group would be a good position irrespective of the outcome of the vote, however, the result may have an effect on the nature or the volume of business that the combined group carries out.

The board of UK TopCo will have equal representation from Deutsche Börse and LSEG. Following completion of the merger, Xavier Rolet will step down as CEO of LSEG, becoming an advisor to the chairman and deputy chairman in order to help facilitate a smooth transition. The arrangement expected to last up to a year.

Donald Brydon, current chair of LSEG, will become chair of UK TopCo, and Joachim Faber, current chair of the supervisory boards at Deutsche Börse, will become deputy chair and a senior independent director.

Deutsche Börse CEO Carsten Kengeter will be CEO of UK TopCo, while LSEG CFO David Warren will move to the same position at the combined group.

Brydon said: "Xavier Rolet has been the architect of LSEG's considerable value creation and has offered to retire in order to ensure the successful creation of the new group. The board of LSEG is indebted to [him] for this action, which is consistent with his focus on putting the interests of shareholders and clients first."

The group will maintain headquarters in London and Frankfurt, and regulated entities within the group will remain unchanged, subject to customary approvals and final regulatory approvals.

The merger is expected to be completed either at the end of 2016 or in Q1 2017.

Rolet said: "We are creating an industry-defining combination which will be a leading global market infrastructure business, very well positioned to create new benefits and efficiencies for our customers and increase value for our shareholders."

"Our highly complementary businesses will accelerate growth. Our shareholders will also benefit from substantial cost and revenue synergies," he explained.

"The combined group will continue to be fully committed to the real economy, by supporting companies, including the 23 million small and medium-sized enterprises across Europe that drive economic growth and job creation. We will create a European leader in global markets infrastructure."

Kengeter commented: "Strengthening the link between the two leading financial cities of Europe, Frankfurt and London, and building a network across Europe with Luxembourg, Paris and Milan will strengthen European capital markets."

"It is the logical evolution for our companies in a fundamentally changing industry."

He added: "It brings together two of the most respected and successful market infrastructure providers in the world to lead the way in European capital markets and set the benchmark for further growth and best-in-class services."

EU and US adopt CCP equivalence

The European Commission has formally acknowledged US central counterparty (CCP) regulation as equivalent to the EU.

The belated agreement follows three years of negotiations between the European Commission and the US Commodity Futures Trading Commission (CFTC) that led to the 10 February announcement by commissioner Jonathan Hill and CFTC chairman Timothy Massad that a common approach for transatlantic CCPs had been provisionally agreed.

Commissioner Hill, who is responsible for financial stability, financial services and capital markets union, said: "This is an important step forward for global regulatory convergence and implementing our agreement with the CFTC."

"It means that US CCPs, once recognised by European Securities and Markets Authority (ESMA), can continue to provide services to EU companies. We look forward to the CFTC's forthcoming decision on substituted compliance which will allow European CCPs to do business in the US more easily."

Most notably, equivalency means that EU banks' exposures to US CCPs will be subject to a lower risk weight in calculating their regulatory capital.

This decision will ensure that both EU and US CCPs operate to the same standards and at a comparable level of cost to their participants, according to the European Commission.

It alleviates the regulatory burden for US and EU CCPs, allowing compliance with only one set of rules.

The aim of this is to encourage market certainty and cross-border activity, while avoiding fragmentation of markets and liquidity.

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A CCP's EU equivalency assessment begins when a country seeks recognition from ESMA.

The applying country's regulator must be able to show that its rules achieve the same objectives as in the EU, although the European Commission has stressed that an identical framework is not necessary.

The US decision follow previous determinations of equivalence made in October 2014 for Australia, Singapore, Japan, Hong Kong, Canada, Switzerland, South Africa, Mexico and South Korea.

Russia and Turkey earn compliance gold standard

Russia and Turkey have been awarded the highest possible grade for their adherence to the Basel risk-based capital framework and the liquidity coverage ratio.

The Basel Committee on Banking Supervision has published a series of reports assessing the quality of regulatory implementation within the two countries as part of its regulatory consistency assessment programme.

The committee rated both countries as 'compliant', the highest of four possible ratings, for their domestic implementation of their risk-based capital frameworks, which were considered to be in line with the liquidity coverage ratio standards.

Several aspects of the domestic rules in both countries are actually more rigorous than required under the Basel framework, according to the committee.

The regulatory consistency assessment programme analyses a jurisdiction's adopted standards and the significance of any deviations from the regulatory framework.

But the programme does not take a jurisdiction's bank supervision practices in to account or evaluate the effectiveness of the regulatory capital and high-quality liquid assets for individual banks or the banking system as a whole.

Record-breaking future trading day for CME Group

CME Group smashed its foreign exchange futures and options trading volume record by 6 percent on 10 March.

The US options and futures exchange achieved trading volume of 2.5 million contracts, surpassing the previous record of 2.3 million set on 6 May in 2010.

Euro foreign exchange futures (euro/US dollar) drove the record day with $127.13 billion in notional traded in futures and $18.5 billion in options. CME Group foreign exchange futures and options contracts are listed by and subject to the rules of the Chicago Mercantile Exchange.

Bears on the rampage in London

Short sellers are turning their attention to London's luxury property market after the five-year growth of high-end housing finally faltered, according to Markit.

Berkeley Group, whose developments are almost exclusively located within London and its commuter belt, was the main target of the bearish sentiment.

The developer's outstanding shares on loan shot up to 6 percent in recent weeks.

"Short interest in Berkeley has since settled slightly to hit 5.2 percent of shares outstanding, but the pace of the reversal is rather stunning given that the current short interest is five times that seen at the start of the year," commented Markit analyst Simon Colvin in a research article.

"This bear raid, which comes at the heels of a 20 percent fall in Berkeley's shares, represents the first time in over five years that short sellers took a position of more than 5 percent of shares outstanding in a UK-listed homebuilder," Colvin added.

Markit research shows that, overall, the property sector is slowing.

The February Markit/CIPS UK Construction PMI Housing Activity Index showed that the sector registered its slowest rate of growth in nearly three years.

Colvin noted, however, that the rest of the UK's property sector is yet to feel the full effects of this market shift, as the average short position among the other 14 UK-listed homebuilders stands at only 0.6 percent.

Only one other firm, Redrow, has seen more than 2 percent of its shares out on loan.

ESMA welcomes comment on SFTR

The European Securities Markets Authority (ESMA) has released a discussion paper on the level two measures of the Securities Financing Transactions Regulation (SFTR).

The window for responses will close on 22 April, at which point ESMA will consider the feedback and publish a consultation paper early in Q3 2016. ESMA's final report and its draft technical standards will be submitted to the European Commission for consideration by 13 January 2017.

SFTR, which came into effect in February, aims to to enhance the transparency of securities financing markets.

The rules follow the Financial Stability Board's framework under which details of SFTs can be efficiently reported to trade repositories.

Do you have a story we should be covering? Let us know via:

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Making your Markit

Markit managing directors of securities finance Edward Marhefka and Pierre Khemdoudi discuss the journey to becoming a cross-asset player in financing

Markit is hosting its 16th Securities Finance Forum on 19 April. What should the attendees look forward to?

Pierre Khemdoudi: We have been hosting our Securities Finance Forum for 16 years now. The forum is very important for both us and our customers as it is a great place to hear from industry leaders about what is currently making the market and where it is heading. This year we have the privilege to open the forum with a keynote speech from James Clunie, manager of the Jupiter Absolute Return Fund, who will share his views on whether funds should short in all market cycles or just in bear markets.

This will be followed by a panel composed of sell-side and buy-side firms who will share their views on the keynote topics. The second panel will discuss the liquidity challenges in the securities finance markets, and we will close the forum with an industry leader panel on how the market should re-think strategies for the future.

Markit Securities Finance has recently released a research paper highlighting the importance of securities lending data for fund managers—can you tell us more?

Khemdoudi: The research paper is called Factor Crowdedness and was released at the beginning of March. In coordination with the Markit Research Signals team, we looked at how the Markit Securities Finance dataset can provide an effective measurement of factor crowdedness.

The paper shows how growth stocks were heavily shorted as compared to value stocks prior September 2014, after which the opposite occurred. From July 2014, shorting highly utilised value stock generated a 38 percent annual return. Combining it with buying lowly utilised value stock increased the return to a hefty 50 percent return on an annual basis. The performance remained strong after accounting for borrowing costs.

Is this the first research paper of a series?

Khemdoudi: In the past we have released research papers in collaboration with market participants. However, we have since started to put together a quantitative research team within Markit Securities Finance. They first released a fixed income paper on signals in the US dollar investment-grade corporate bond market, combining our securities finance dataset with Markit's extensive fixed income data.

As we are now growing the team, we are increasing the frequency of our research papers. For example, to mark the fact we will shortly have a complete 10 years of daily history, we are working on a paper that will review the performance of our key data points and discuss reasons why the signals performed well or poorly in different macro environments.

The second session of the forum will focus on liquidity challenges in the securities finance market—can you elaborate?

Edward Marhefka: In this session we intend to discuss how liquidity issues are affecting the securities finance market. The repo market is the primary source of short-term funding for banks and an important short-term investment vehicle for money market funds and cash reinvestment for securities lenders. However, myriad regulations are forcing a retooling of the repo market's gears, and will disrupt market participants and liquidity flows until completed and fully digested by industry participants.

Furthermore, Basel III's risk capital and the more stringent US enhanced supplemental leverage ratio requirements have cumulatively encouraged banks to drastically modify their business models with regards to capital, assets and balance sheet. Banks have shed assets, particularly of the risk-free, lower yielding types such as repo, leading to reduced capacity to fulfil client requests to cover shorts (when not in inventory) and the availability of high-quality liquid assets.

Additionally, we will discuss the reduced liquidity in the corporate bond market and the consequences for the securities lending market.

Is Markit Securities Finance leveraging other Markit products to help its customers navigate the corporate bond liquidity maze?

Marhefka: That is correct. Markit Securities Finance has integrated some of the components of the Markit bond pricing suite. For example, by combining the securities finance dataset with the Markit Liquidity Scores, our customers can evaluate quickly the liquidity of a corporate bond and therefore manage better the risks in lending and/or borrowing them.

Blockchain is hot topic in the financial markets at the moment. Is Markit Securities Finance looking into this technology?

Marhefka: Indeed. Many banks have publically announced their initiatives in this space and much has been published around this topic. However, many of our customers are asking us questions about what this means for the securities finance markets. We therefore decided we should do a session on blockchain as part of our forum to explain, simply, what blockchain could bring to the financial markets and, especially to the securities finance markets. We believe that if adopted, this would have a profound impact.

It seems that you have avoided the traditional regulatory session when planning the forum. Is there any specific reason for that?

Marhefka: It is clear that regulation is an important topic. However, as the recent regulatory onslaught is being digested, the market is being reshaped and regulation is simply becoming part of how the market behaves. Although we do not have a specific focus on this topic, regulation and its intended or unintended consequences will be discussed throughout the afternoon.

As implementation of SFTR is coming closer, how do you think the market is preparing itself?

Khemdoudi: The Securities Financing Transactions Regulation (SFTR) is an interesting part of the recent regulatory changes. The overall framework is pretty daunting and we are seeing a very disparate level of preparedness among our clients. I take this occasion to praise the work of International Securities Lending Association and European Repo Council, which are pulling all of the industry around this as it is very clear that the industry is in need of a solution.

At Markit, we have provided over-the-counter (OTC) services including regulatory reporting to our clients for several years now. By combining the experience developed in OTC reporting with the Markit Securities Finance dataset, we will be able to provide the required fields that are needed for SFTR.

We therefore believe we can help our clients to comply with this regulation quite quickly, should they want to utilise our services.

You are about to release new features for the Markit Securities Finance product. Can you tell us more?

Khemdoudi: We are releasing a new metric that will help our customers gauge the overall stability of the inventory, at the security level. We are very proud of this feature as it has been devised by our newly created quantitative research group. Thanks to the breadth of our data, we are able to assign a degree of stability to each of the underlying funds populating the inventory.

Using this new metric, our customers will have additional and never before seen information to assess the risk of their positions. We are also continuing to add new features to our benchmarking tools, addressed to the lenders' and beneficial owners' areas of the market.

Are you about to release global intra-day securities lending data?

Marhefka: That is correct. We have been beta testing the intra-day dataset with some of our clients. We are coming to the end of the testing phase and will be ready to release a global intra-day dataset very shortly. This will allow our clients to get more timely data across the globe. As usual, this is a give-to-get dataset, so to be able to see the data, our clients will need to provide us with their intra-day data.

We understand that you are also expanding your consultancy team?

Marhefka: Historically, our consultancy business has been managed solely out of London. We believe that with the upcoming regulatory challenges, a US presence is necessary so we can offer a truly global service to our clients and efficiently expand our customer base. We have therefore asked Steve Baker, based in New York, to co-manage our consultancy branch, along with Sandra Fernandes who is based in London.

What does the future hold for the securities finance market?

Marhefka: This is what we are going to try to answer in the third panel of our forum. With low interest rates, balance sheet constraints and additional regulation, it is clear that certain historical avenues of revenues have been drastically reduced. However, collateral optimisation, increased short balances and cross-asset strategies should help create new avenues of revenues.

How will CoreOne fit into your strategic efforts in the financing space?

Khemdoudi: The acquisition of CoreOne technologies at the end of last year is reinforcing Markit's presence in the secured financing space and affiliated markets. Through this acquisition, Markit acquired the DeltaOne solution, which completes existing Markit products providing index management services along with exchange-traded product data and dividend forecasting analysis. Combining these with securities finance data will allow us to offer a truly unique service addressed not only to the sell side but the buy side, too. Edward Marhefka and I are global co-heads of the division.

Since the beginning of the year, the teams have been busy migrating all legacy Markit customers into the newly built DeltaOne platform so we can offer our premium products to our customers. Additionally, thanks to this acquisition, Markit is now able to offer a complete cash and synthetic prime brokerage platform with PrimeOne. All of these products service the financing space, so making sure that they all talk together will help us to position Markit as a major cross-asset player in the financing space. **SLT**

First mover disadvantage

The EU moved first with its reporting requirements for SFTs, but beating other FSB members to the punch might have been a mistake. Paul Landless of Clifford Chance and Greg Lyons of Debevoise & Plimpton report

How has the EU's regulatory framework developed?

Paul Landless: The EU's view and priorities may be viewed as broader to the Financial Stability Board's (FSB) goals of addressing financial stability risks.

The EU's rules for reporting under the Securities Financing Transactions Regulation (SFTR) is very wide in that it captures any European entity's activity, whether or not it is regulated by the EU. There are issues on product scope as well. Lending money for acquisition financing where the target's shares are given as securities could trigger some requirements, even though it's a relatively day-to-day corporate transaction. Some types of margin lending could be caught up in this too.

I don't think the FSB had a reporting system like this in mind—one that picked up all and sundry. As well as being more very broad in some areas, the two-year phase-in of some of the EU's SFTR rules is underway already and is being implemented faster than other FSB members, many of which have not proposed equivalent rules.

How much scope is there for discrepancies in sanctions on reporting?

Landless: A lot of the regulation in Europe, such as the European Market Infrastructure Regulation (EMIR) and SFTR, can hand over enforcement to member states. SFTR is a regulation with a capital 'R' and not a directive needing national implementation, so everyone is using the same rulebook, but the differences come in the rigidity of enforcement by each member state. For example, the French regulator could have a very strict compliance view compared to the German regulator if it sees operational failings. It could be a matter of resources if carrying out these rules requires a large IT investment or increasing your headcount.

> ***I don't think the FSB had a reporting system like the EU's SFTR in mind—one that picked up all and sundry***

Paul Landless, Partner, Clifford Chance

Given the potential for overlap leading to an overbearing regulatory environment, has there been much push back from the industry?

Greg Lyons: In Europe and Asia, there are reports citing material concern by certain governments and government agencies that the Basel Committee on Banking Supervision has published a broad array of rules since the financial crisis without reconsidering the aggregate impact of those rules or whether their objectives are consistent.

For example, in November of last year, Bank of England governor Mark Carney indicated that "it would be a miracle if all that regulation … perfectly fit together so that there was no duplication … and no contradictions".

Similarly, earlier this year, Denmark's ruling Liberal party voiced the concern that by simply adopting the Basel standards without adjustments, Europe had put itself at a disadvantage to US banks.

The Swedish Financial Supervisory Authority and the chair of the European Banking Authority have also raised questions about the need for adjustments in the rules, and in Asia, the Japanese Financial Services Agency has also indicated that the impact of Basel III may be too large.

In the US, on the other hand, the regulators appear to be doubling down. Last year, Janet Yellen, chair of the Federal Reserve, said in congressional testimony: "Capital charges are causing firms to think seriously about whether or not they should spin off some of their enterprises to reduce their systemic footprint … And frankly that's exactly what we want to see happen".

Due to the concern around some aspects of SFTR, is there still time to negotiate some of the more controversial points?

Landless: The main body of the regulation is already in force. The things we need to get more details on are all the specific rules around reporting. Questions to do with how you report trades, what goes in reports and how to license different trade repositories all still need to be answered.

However, at the moment there is no guarantee that the European Securities Markets Authority (ESMA) will add any more colour to the other rules on increased marketing disclosure and account reporting around a fund's SFT usage for investors, and therefore it is very unclear what consultation or negotiation is feasible, on any of it.

On the other hand, there is no room to manoeuvre around the rules on collateral re-use with the trade documentation requirements for disclosure and proper execution going live in July. **SLT**

> ***The Swedish Financial Supervisory Authority and the chair of the European Banking Authority have also raised questions about the need for adjustments in the rules***

Greg Lyons, Partner, Debevoise & Plimpton

Understanding CSDR in detail

The settlement discipline regime of CSDR, as proposed, might actually make failure an option, according to Matthew Johnson of DTCC

The industry has now had the time to familiarise itself with the final level two regulatory technical standards tackling settlement discipline under the Central Securities Depositories Regulation (CSDR). The European Securities and Markets Authority (ESMA) published the final text on 2 February without much fanfare, even though this piece of the regulation is possibly the most far reaching of all, as it spans from trade capture all the way through to trade settlement, encompassing the entire trade lifecycle.

Measures to prevent trade fails include standardised information to be captured in trade confirmations, endorsement (but not mandating) of electronic mechanisms to dispatch confirmations and allocations, as well as to provide this entire detail in a written format. These are commendable efforts, even if monitoring the industry's adherence to the mandated rules might prove somewhat challenging.

Arguably, one of the most interesting aspects of the regulation is the introduction of penalties for transactions that fail to settle on the intended settlement date. CSDR will penalise those market participants that are unable to deliver securities or cash within the T+2 timeframe. Each failed trade will incur a daily charge on the notional value of the transaction for each day the trade fails, up until the mandatory buy-in period—although the buy-in inclusion is another conversation all on its own.

This sounds punitive, as many European markets currently do not have standard trade failure penalties. This could make trade failure a costly business—or does it? The vast majority of market participants support harmonised trade failure penalties as they believe it will lead to an improvement in performance, including enhanced focus on straight-through processing (STP), and the electronification of trade confirmation and settlement. But when we take a closer look at the size of these penalties, they may not have the desired effect, which might explain why so many market participants were in strong support of them.

For example, if an institution fails to settle an equity transaction for whatever reason, the fail will incur a 1 basis point (bps) charge on the notional value of the transaction. If we put this into figures, an equity transaction worth €100,000 will incur a €10 penalty for each day that it fails, so not a very steep penalty. That said, however, ESMA's decision to keep the penalty costs low was factored into the cost of borrowing. If an institution is short to deliver they can borrow to cover the position. And of course, borrowing comes at a cost. Many larger institutions have auto-borrow processes in place, even if it is more expensive than manual borrowing.

> ***The settlement discipline regime of CSDR could actually drive-up failed trade rates rather than decrease them***
>
> **Matthew Johnson,** Manager of EMEA industry relations, DTCC

So, with these economics in mind, will the settlement discipline regime work in practice? Failed trade costs, as well as borrowing costs, all affect the bottom line of a dealer's trading book for which heads of dealing are ultimately responsible. As a head of dealing, you may give approval to the operations team to setup auto-borrow agreements with as many custodians as possible. For example, the cost of auto-borrowing may be 50 bps—this means that settling trades on time costs 50 bps while the price of letting them fail under ESMA's proposals is only 1 bps. Potentially, one could save 49 bps by letting the trades fail. As the rules currently stand, there is a serious risk that this may happen. If so, it will be a stark example of the unintended consequences of regulation. As a result, the settlement discipline regime of CSDR could actually drive-up failed trade rates rather than decrease them, therefore defeating the very purpose it has set out to achieve. **SLT**

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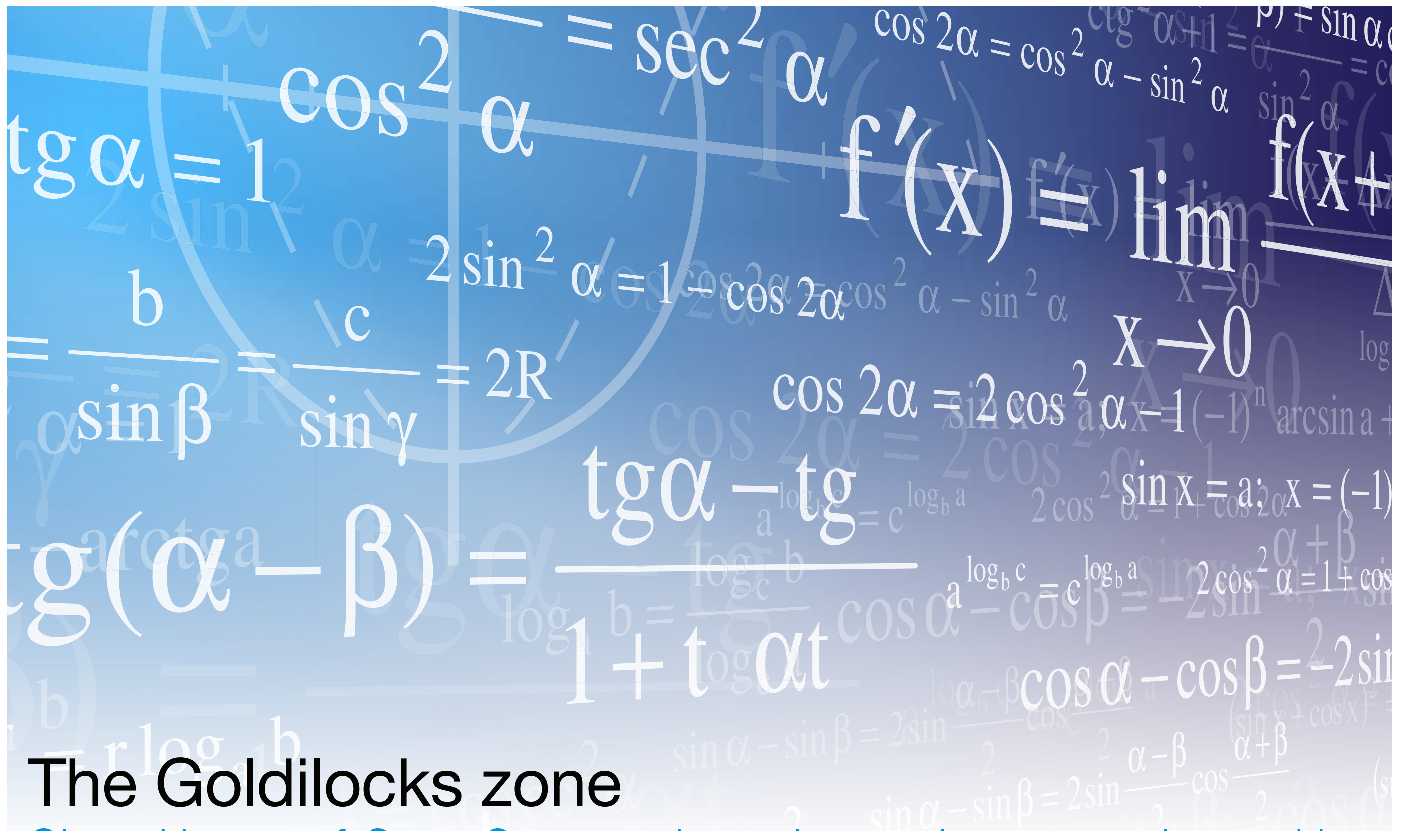

The Goldilocks zone

Glenn Horner of State Street reviews the newly proposed securities financing transaction standardised calculation, finding it to be just right

Following the financial crisis in 2008, global regulators were presented with an unenviable task of rewriting banking regulations in a sensible manner while adhering to a number of core principles.

Among the guiding principles, measures should:

- Be simple enough to be easily understood and implemented across banking organisations;
- Be conservative enough to capture potential risks in a stressed market environment;
- Reflect the actual potential future exposure a banking entity might incur;
- Be risk sensitive; and
- Across similar economic exposures, be similar in magnitude so as to avoid regulatory arbitrage.

Historically, for securities financing transactions (SFTs), many of the largest agent lenders utilised a simple value-at-risk (VaR) measure to calculate the potential exposure-at-default (EAD) for each counterparty. As a result of the financial crisis, however, the use of such simple VaR measures came under greater scrutiny from global regulators. The primary objections to the use of a simple VaR measure were: (i) the relative complexity of the models utilised; and (ii) the fact that different banks reported different EADs for similar loan and collateral portfolios.

Additionally, despite agent lenders reporting no losses due to their loan indemnities, many regulators believed that the simple VaR models resulted in EADs that did not fully reflect the potential risks of a stressed market.

As a result of concerns that the various internal models for simple VaR did not reflect stressed market conditions and the lack of comparability across firms, regulators have explored utilising a standardised floor for banks that calculate risk-weighted assets (RWA) under an advanced approach.

Under the Collins Amendment to the Dodd-Frank Act, the largest US banks are required to calculate RWA under both the advanced and standardised methods and to manage to the more conservative of the two at the firm-wide level. The Basel Committee on Banking Supervision is exploring a similar floor on a global basis. Additionally, the standardised method has been proposed as the method to calculate exposures under both the single counterparty concentration limits (SCCL) in the US and Basel's large exposure limits. As such, the importance of the standardised method has increased significantly, even for those advanced approach banks that have historically utilised a simple VaR measure for calculating SFT exposures.

The existing standardised approach for SFTs meets regulators' goals of simplicity, consistency and conservativeness. However, it fails on the other key criteria, namely, risk sensitivity and reflection of actual exposures that may be incurred even under stressed market conditions.

Further, the resulting EAD for SFTs varies substantially from the EAD that would be calculated for derivative transactions with identical or very similar economic exposures. These deficiencies are driven primarily by the standardised approach's lack of consideration for correlation and diversification benefits within a portfolio of loans and collateral. The existing measure relies on a set of additive haircuts for both loan and collateral positions even if these positions are largely offsetting.

As a simplified example, suppose a lender lends Apple shares worth \$100 and receives Intel shares worth \$105 as collateral. The current model assumes that, in the event of a counterparty default, the Apple shares would increase in value by 10.6 percent over the five-day buy-in

horizon while the Intel shares would decrease in value by 10.6 percent during the same period.

Example EAD using existing standardised approach, equity versus equity loan:

= (Assumed higher value of Apple shares) – (assumed lower value of Intel)
= ($100 *(1 + 10.6 percent)) – ($105 *(1 – 10.6 percent)) = $16.73
= $16.73 / $100 (original loan value) = 16.73 percent

This hardly seems plausible and becomes even more unrealistic when one considers that many loan and collateral netting sets include hundreds or even thousands of positions. In fact, estimates from market participants indicate that the EADs from the existing standardised approach are 20 to 30 times higher than EADs calculated using a simple VaR model.

With these considerations in mind, the Basel Committee on Banking Supervision has proposed a new standardised methodology for SFTs utilising the following formula:

EAD = |(0.4 * net exposure)|+ (0.6 * gross exposure/√N)

Where:

- Net exposure would allow for the offsetting of collateral and loan positions, reflecting the systemic risk of the portfolio;
- Gross exposure would be cumulative across loans and collateral, reflecting the idiosyncratic risk of the portfolio positions; and
- N represents the number of securities in the portfolio (with some relative size requirements).

In addition to the proposed new formula the Basel Committee on Banking Supervision proposed raising certain haircuts.

The new haircuts for a five-day holding period for main index equities would be 14.4 percent. If we used our prior example, the new EAD would be as follows:

EAD using proposed new standardised approach, equity versus equity loan:

= |0.4 *($100*14.4 percent - $105*14.4 percent)| + (0.6 * ($100*14.4 percent + $105*14.4 percent)/√2)
= 0.28 + 12.52 = $12.80
= $12.80 / $100 = 12.8 percent

We would see a marginal benefit under the example. However, the benefits would be further magnified as the portfolio of loans and collateral increased. Early estimates by market participants indicate that average EADs would decrease by approximately 70 percent using the proposed new formula.

While markedly lower relative to the existing standardised approach, EADs under the proposal would still be very conservative at approximately five to seven times higher than the EADs calculated under a simple VaR method.

Overall, the new proposal by the Basel Committee on Banking Supervision is quite remarkable in that it meets all requirements for a sound regulatory measure.

It maintains a conservative estimate of EAD that is relatively simple to understand and implement across different organisations, and it represents the potential impact of a stressed scenario.

Further, it addresses key shortcomings of the existing standardised measure since it is also risk sensitive, represents actual potential future exposures and eliminates the significant difference in measurement for like economic exposures under derivative and cash-based trades.

With the new standardised approach proposal for SFTs, the Basel Committee on Banking Supervision has truly identified a Goldilocks solution: one that is not too complex for most users, but which represents a conservative yet reasonable calculation of EAD.

While this solution, if implemented, would result in a calculation that meets the key regulatory objectives it should be noted that it is only a proposal from Basel.

Until such time as it is adopted in the US, large banks will still be required to calculate their risk-based capital calculations on both the advanced and current standardised approaches due to the Collins Amendment of the Dodd-Frank Act.

Once finalised by the Basel Committee on Banking Supervision, the proposal would have to go through a similar process within the US whereby regulators would put out a proposal, receive comments and then ultimately finalise the new calculation.

Obviously, with the multiple steps for adoption there may be resistance at some levels and it will likely be a multi-year process. **SLT**

With the new standardised approach proposal for SFTs, the Basel Committee on Banking Supervision has truly identified a Goldilocks solution

Glenn Horner, Managing director, State Street

In a dark, dark market

Is the so-called collateral shortfall a result of asset hoarding, excessive regulation, or simply a tall tale told to young bankers before bedtime?

Is the liquidity crisis reality or fiction?

Scot Warren
Executive vice president of business development
OCC and the Options Industry Council

Reality. From OCC's perspective as a central counterparty (CCP), we are seeing increased capital requirements affecting market behaviour. Due to their increased capital requirements, clearing firms are being more stringent with the credit they extend to liquidity providers and the balance they are allowed to hold. In turn, liquidity providers display less liquidity in the market. For other market participants, lower liquidity levels increase their implementation costs, therefore reducing the value of using CCP-cleared products. Diminished value for investors leads to lower demand for listed products.

Additionally, for CCP's the cost of securing committed credit facilities is increasing and has become more challenging due to being included in single counterparty exposure limits. As a result, OCC is pioneering paths to finding new sources of liquidity by working with public pensions.

Joseph Gillingwater
Head of international fixed income trading
Northern Trust

The large premium to borrow the current 10-year US treasury bond in repo markets and subsequent rise in failed trades, as noted by the Federal Reserve Bank of New York, has understandably received a lot of coverage. Meanwhile, the European Central Bank (ECB) maintains its presence as a large buyer of sovereign debt under its asset purchase programme, recently increasing the size and expanding the list of eligible assets to include corporate bonds.

Concurrently, regulation has forced banks to compete with the ECB and hold large inventories of high-quality debt rather than lend in the repo market, while institutions continue to shrink balance sheets and shift away from less lucrative and capital intensive business. However, we take comfort from the recognition of the issue from global central banks, while maintaining our position at the forefront of market evolution for initiatives to mitigate any liquidity risks.

Michael Landolfi
Securities finance product and strategy manager, markets group
BNY Mellon

The 'reality' of the liquidity crisis is beholden to an individual's definition of liquidity crisis. If one defines a liquidity crisis as a firm's inability to obtain needed liquidity in a timely manner, then market evidence is indicating that currently no significant liquidity crisis exists.

If one defines a liquidity crisis as an environment where the liquidity resource has limits and constraints subjecting it to escalating prices and alternative sources, then evidentiary market data is indicating that a liquidity crisis may be developing with the implementation of regulatory reform and the reactive measures that financial institutions are adopting to comply with this new regulatory environment.

Financial institutions that recognise and innovate around this new emerging liquidity environment will be best positioned to succeed going forward versus their peers.

Karl Wyborn
Managing director, global head of sales
CloudMargin

Liquidity crises are not uncommon. We have witnessed several significant, acute reductions in liquidity in the periods during and after many of the crises that have peppered the last 20 years of financial market activity. These were neither structural nor chronic in nature, however. In contrast, what we witness today appears to be a structural reformation of the markets driven by new regulations. The marked decline in liquidity in US treasury repo over the last 24 months, during a period of otherwise buoyant economic growth, reinforces that the current challenges, while not yet endemic, are not simply an acute reaction to underlying economic weakness.

The real fear, however, is the impact of forthcoming regulations rather than what has passed before. The further implementation of Basel III, the migration to central clearing of over-the-counter derivatives and the exchange of initial margin on non-cleared derivatives will further reduce liquidity as banks, among others, hoard sovereign debt to meet their regulatory obligations. This is a widely anticipated and foreseen impact of regulators' response to the global financial crisis. The 'real' question, therefore, is the extent to which regulators want to reduce liquidity.

James Treseler
Global head of cross-asset secured financing
Societe Generale Prime Services

We find that many institutions are struggling with applying the short- and medium-term liquidity ratios at a business line level.

But it is far from a crisis. However, it is worth noting that the industry, specifically the repo markets, have experienced exceptional squeezes on collateral. These events can be described as one-offs, not systematic at this stage.

Steve Baker
Director, securities finance
Markit

If we define liquidity risk in terms of funding, the risk of being unable to settle obligations with immediacy over a specific time horizon, we see several factors pushing in opposite directions and into cash market liquidity risks.

The repo market is the primary source of short-term funding for banks and an important short-term investment vehicle for money market funds and cash reinvestment for securities lenders. However, myriad regulations are forcing a retooling of its gears, disrupting market participants and liquidity flows until completed and digested—at least we hope.

Basel III's risk capital and the more stringent US enhanced supplementary leverage ratio requirements have cumulatively encouraged banks to drastically modify their business models with regards to capital, assets and balance sheet. Banks have shed assets, particularly of the risk free lower yielding types such as repo, leading to reduced capacity to fulfil client requests to cover shorts (when not in inventory) and availability of high-quality liquidity assets (HQLA).

And while banks are required to secure longer term durable funding, Rule 2a-7 funds now have shorter weighted average maturity and higher stress testing requirements that have disrupted the historic symbiotic relationship between the two. To some degree, beneficial owners in the securities lending market are picking up the torch by accepting more alternative collateral types and longer cash reinvestment terms.

Our data has shown a significant and sudden rise in the use of evergreens since Q1 2016 within the US triparty market. In particular, with non-Fedwire eligible asset types such as equities and terms

exceeding 30 days. This is encouraging and shows that banks are achieving greater operational efficiencies to term out funding and meet the new regulatory requirements. But what about those cash investors who seek short-term high quality collateralised investments and can no longer be serviced by banks?

Key questions remain open for the future of funding liquidity such as whether more of these traditional bank customers can join central clearing, or use peer-to-peer and direct repo and lending routes.

Nick Nicholls
Principal consultant
GFT

A liquidity crisis is very likely and is attributable to the impact of banking regulation on bond market demand. What holds this back today is that for the most part, we have quantitative easing in most large economies, with enforced low interest rates.

The impacts of capital regulations and leverage ratios mean that banks have less scope to hold higher yielding corporate assets. The result is that credit markets are constricted.

HQLA yields—driven down as a result of banks needing to hold reserves to meet liquidity ratios, and (from September) for initial margin on non-cleared derivatives—aren't immune from a liquidity squeeze.

In a global economy where secondary market demand is constricted, a rate hike (as expected in the US) could see sellers without buyers of any size. The resulting fall in asset values will affect the HQLA reserves that banks are obligated to hold, leading to further loss of bank's credit value.

Ted Leveroni
Chief commercial officer
DTCC-Euroclear GlobalCollateral

Once global derivatives regulations are fully implemented, there will be localised liquidity challenges—either firm to firm or region to region. However, at a macro level, there is sufficient liquidity in the financial system. This disconnect between the macro and local level is due to the large number of collateral bottlenecks caused by limiting characteristics in financial market infrastructure.

These bottlenecks lead to eligible collateral becoming immobilised in one part of the system, making them unattainable for market participants that need access to their inventory of collateral for central clearing and higher margin requirements for bilateral transactions.

Eliminating this disconnect is key to avoiding a liquidity crisis and will require cross-border collaboration and the development of holistic, industry-wide solutions that allow firms to process and track their collateral, which will then facilitate centralised, automated collateral optimisation. Only then can the industry mitigate liquidity risk and solve the collateral challenge. **SLT**

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Build or buy?

The in-house versus vendor debate polarises opinion. Consolo senior partner Richard Colvill speaks to four experts to see where the answer might lie

You've concluded that your legacy platform is creaking at the seams, no longer fit for purpose, un-scalable and rapidly approaching the end of its life. Or, you're a new business start-up and the world's your oyster. In both cases, the million dollar question, or as is in many cases, much, much more, when deciding on a new system to support your business, is, do you build in-house or purchase from an established vendor. This is a question that polarises opinion.

This is likely to be a conundrum discussed at great length by every establishment in the financial industry, and one that quite often spans a period of many weeks, months and years. Unless you've experienced it for yourself, you probably have no appreciation of how big a challenge this is. But those that have will testify that you would only want to do it once in your career. Unless, of course, you're one of those change management or project management types, because they love it.

This is a task that is exacerbated in the larger firms where the number of stakeholders with differing opinions is far greater than in their smaller counterparts. The emails, the think-groups, the breakout area, manager's office, clandestine chats over the coffee machine—it goes on and on.

While this decision ultimately rests with the board of directors and executive management, the key influencers reporting to these levels can be many in number and often with differing opinions and agendas. Trading, client, marketing, product, strategy, operations and IT managers will all have different objectives, such as increased volume, automation, profitability, scalability, job security, shareholder value, cost, support, development and flexibility, to name a few.

And so the process begins: whitepapers, proposals, business cases, feasibility and affordability studies, return-on-investment analysis, due-diligence and market research. The amount of paper seems endless, and it must all be juggled around your day-job (thank you very much).

Eventually, judgement day arrives and hurrah, a decision has been made. The lucky (or more influential) ones get their desired result while the others suffer an unbearable loss of professional pride. The victors soon lose the sweet smell of success from their nostrils, when they see how insufferable the 'no' voters become for the duration of the rest of the project. Still it was nice while it lasted.

So, of in-house and vendor, which option is the best option? There are many factors that underpin the question, including: the speed at which it needs to be delivered; the cost; the risk; the knowledge, resources, capacity and infrastructure to support it; the up-tick; and people.

Sunil Daswani, senior vice president and head of international securities lending at Northern Trust Global Investors, provides his views on the decision to build in-house.

Global Securities Lending (GSL), Northern Trust's securities lending proprietary trading system, is a single global 24/7 platform. It is a multi-function system for managing the securities lending business end to end.

GSL has electronic links in place to depositories, other securities lending vendors, custody systems, and EquiLend. The electronic links we have in place with borrowers, both direct and through EquiLend, automate the majority of loans. On average, 90 percent of our loan volume is automated without manual human intervention.

We also use similar automation via GSL for our post-trade reconcilement and mark-to-markets to be more efficient and maintain strong risk management. GSL was implemented in 2003 and we routinely enhance the system to meet new business requirements.

Having an in-house system means we can normally bring new variations of the product, set up lending in new markets and build customised solutions for clients in a manner that can transfer to be scalable in the future, should there be demand.

The decision we made to go in-house has certainly paid off given the large amount of new business we have brought in where we have capabilities that some of our peers may not have. Additionally, our peers may experience delays to-market for new or enhanced product offerings where off-the-shelf packages are used, which in our view gives us a major strategic advantage.

So a global custody agent lender leaves us in no doubt why the decision to build internally was the right one.

Bill Foley, director at securities finance specialist Foley O'Neill, and, with a wealth of knowledge gained at a number of leading market participants, shares his thoughts on past experiences of both developing in-house and outsourcing to a vendor.

Having been through the process of implementing both off-the-shelf and in-house built securities finance systems, I have seen the merits and pitfalls of both. Plug-and-play solutions can sometimes offer exactly the speed and ease that the name suggests, but it can also sometimes seem more like 'plug-and-pray' once the implementation process begins.

Similarly in-house builds should, in theory, see IT departments able to use their knowledge of the business and existing systems to build something bespoke in a cost-efficient and timely manner, and many are able to achieve this. However, without a full and honest appraisal of internal resources, skills and required connectivity to other internal platforms, in-house builds can become fraught affairs, often with much compromise, delay and additional costs incurred along the way, as well as running the risk of the project being re-prioritised, which rarely sees it moved up the list of priorities.

The decision to choose one route over the other will depend on a number of factors that will vary from business to business, so it is impossible to give a definitive view. However, the most important element to arriving at the right conclusion is to ensure that all stakeholders are involved from the outset. This includes both internal and external contributors.

Internally, the business case must be fully understood and supported by all and the entire process must be agreed by all those involved at the outset.

The entire process can often be managed better by utilising the right external resources, whose aim is solely to deliver the right solution and can focus resources completely on the delivery without being sidetracked by their day job. The most successful system implementation that I can recall from my own experience utilised exactly this approach.

Some thought provoking words of wisdom from an established industry veteran, who found that, as far as management of the job is concerned, external resources can be beneficial.

Tom Dibble, head of product management for securities finance at FIS Global, provides a view on why he believes his target audience prefers, and will benefit from, FIS's solution and service offerings.

FIS has seen a significant upward trend as existing and prospective clients move away from in-house development of products and instead move to support services that enable these organisations to focus their resources on critical core business. As a result, there is growing demand for a comprehensive range of services and solutions that FIS offers across the securities finance landscape, all targeted at reducing centralised risk and lowering total cost of ownership.

FIS's established securities finance solution set, such as Global One and Apex Securities Finance, is delivered via a framework of fully managed and domain specialist services. These services encompass the front-to-back business and technical requirements for our partner clients, where the responsibility for the solution environment remains with FIS across a strategic and long-standing service delivery model.

As we use our solution framework to create specific client delivery models, options range across our expertise, from our own data centres, through supporting mechanisms, change project delivery and product knowledge. This multi-strand approach that builds on our years of leading edge expertise in these areas enables us to talk across delivery boundaries and fill the gaps that other products, both in-house and solution providers, can sometimes have.

FIS is a trusted global financial technology partner to more than 20,000 clients across 130 countries. Our intention is always to be a willing and capable partner in helping our customers drive to success and we believe our wide range of services, from product to delivery, across the whole relationship with our customers, is vital and vibrant as we look to the future and empower the financial world.

A compelling argument from a vendor with a long-standing history in securities finance, and which many in the industry would view fondly as the first mainstream systems solution provider with Global One.

Paul Wilson, product director for global sales at 4sight Financial Software, gives his views on the debate.

It's an interesting decision. In fact, the largest competitor to 4sight, and I'm sure to most of our peers in the vendor space, is a combination of doing nothing and building in-house.

Where 4sight does win a mandate to install a securities finance system, it's always to replace an existing in-house system or an older vendor system that has become, on the whole, so ingrained and bespoke that it's effectively in-house. The reasons why an institution might choose to do this is interesting. If I look at the most recent deals that 4sight has won, it's a combination of factors. In order of priority:

1. Fit for purpose (both functionally and architecturally), and the business really wants it;
2. Functionality uplift;
3. Operational cost and risk reduction;
4. Cost effectiveness; and
5. Magic dust.

Ultimately, no-one in their right mind is going to buy the wrong, expensive, ill-fitting spanner for a job that, when applied to a stubborn nut, skins their knuckles painfully every time.

Interestingly, though, many people actually make the decision to hand-forge, finish and deploy their own bespoke spanners from scratch. The problem is that when the standards change, you end up re-engineering it all from scratch each time, and the spanner often doesn't come out quite right, requiring considerable reengineering.

Alternatively, you can buy an off-the-shelf toolkit with a lifetime guarantee, catering for all standards, and with a socket set, ratcheting spanners and free mug all included.

Why would people do anything but the latter?

In my experience, functionality is the key deciding factor, and in fact passing the 'fit for purpose' test is our clients' primary decision. Which means that the tool (in this case 4sight) is fit for the job both functionally and architecturally. Put simply, they wouldn't buy it if it wasn't. Those interested in the hand-forging route truly believe they can build something better than a vendor. This is true for some institutions, but our experience is that this is not a widespread truth and can be a very expensive function, particularly in our ever-changing regulatory landscape.

This decision is often made first by the business owners and their IT owners. Business also tend to see functionality uplift, for example, an improved ability to manage extendables, monitor balance sheet impact, process optional dividends, or achieve full straight-through processing for SWIFT. Interestingly, if the decision is front-office/business-led, a future vision of the 4sight roadmap and the ability to optimise trading decisions is often the key unique selling point, whereas if the decision is more operational or technical, the decision gets much more low level and delves into the architecture of the solution in terms of cost and risk reduction.

Obviously, cost is key. Nothing in life is free, and the old adage of pick two out of good, fast and cheap is paramount. Once procurement are involved, it's a fairly standard negotiating process with the client. The hard part of this is having clients understand that it is difficult to predict the impact of large institutions' reaction speed, bureaucracy, skillsets and access to actual users on project cost. However, on paper, it's fairly cut and dried and a lot cheaper than many institutions might think.

There's a finite set of fairly standard migration datasets, up and downstream integration points, extracts and reports to integrate, plus some inevitable gap development, so it is possible for 4sight to provide capped, fixed-price and surprisingly cost-effective high-quality projects. Factor in dozens of existing clients all feeding into the system and 4sight's clear focus on securities finance, and the future costs are also attractive because, if your vendor is proactive, their system is always on-track with where the market is heading. And it's heading into waters we have never imagined.

One last thing: the magic dust is whether the client considers that the vendor understands them, or that we 'get' the crux of their problem and are convincing, straight up and compelling both now and as a long-term partner.

This is the 'relationship factor' and it's a truth that 4sight ultimately wins deals based on this final, hard-to-quantify consideration.

Having been involved in projects supporting both decisions on several occasions, Consolo knows that the process and challenges from a business or change perspective are practically identical.

The bottom line is that somebody, somewhere, at the top of the decision tree and holding the purse, will draw a line in the sand and demand delivery by a predetermined date and within budget. There's always a little bit of wiggle-room but that good grace is limited and,

in the end, the project will be made to deliver all or most of the requirements on or before that date.

I say 'most' because there is a constant with both vendor and self-build installations. Something is always decoupled from the main delivery and re-phased for a later installment, a victim of the budget and time constraint demands. What was once a 'must-have' becomes a 'nice-to-have' and the term 'workaround' is attributed.

For the end-user, this workaround can be an eternal source of frustration, as popular belief is that it is something that all discerning systems should offer at entry level, yet the truth is it was dropped to meet a deadline, or assumed but never explicitly requested. These workarounds are now thrown into what us change types call 'retrofit' and they are graded according to the business criticality versus development time-lapsed and cost equation versus the time it takes to perform the workaround. Only when this exercise is complete can the vendor or your internal developers prioritise these, subject to the allocation of further resources and budget.

Frustratingly, users will find that these retrofits are now directly contesting with new business and product development inventory for the ever-diminishing budget and resource pool, so some of these may not see the light of day for a very long time, if at all. However, if resourced correctly from the start, and with the business's best interests at heart, these issues can be avoided, ensuring that not only will users get the system that they want, but the system that they need. **SLT**

"The bottom line is that somebody, somewhere, at the top of the decision tree and holding the purse, will draw a line in the sand and demand delivery by a predetermined date and within budget"

Richard Colvill, Senior partner, Consolo

Fully pledged

BNY Mellon is expanding to support demand for fixed income trading in the Asia Pacific, say Howard Field and Paul Solway of BNY Mellon

This year marks the formal expansion of BNY Mellon's global fixed income offering with the addition of dedicated agency trading capabilities out of Hong Kong. The bank is actively committing resources to this capability with a Hong Kong trading desk already in place and operational support scheduled to be rolled out throughout the remainder of 2016.

By the end of the year, BNY Mellon will have a fully functional front-to-back model and be able to trade, support and settle fixed income securities lending trades in the Asia Pacific region. Why venture into fixed income at a time when other institutions are pulling back?

The Hong Kong desk's ability to structure term trades, for example, either via bullet or extendable, also helps to enhance a beneficial owner's fee earning potential. Borrowers and beneficial owners will now have local access to a global inventory, managed by trading desks operating from a unified technology infrastructure around the world.

Throughout the trading day, beginning in Asia and stretching across the globe to the Americas, our technology delivers information for our entire team to utilise in managing our lending book. Fixed income trading is certainly facing some headwinds in today's economic environment, but it's still a growing business in the Asia Pacific.

"The main reason is client focus—serving the needs of borrowers and beneficial owners"

Howard Field, Regional head of fixed income trading for EMEA and APAC, BNY Mellon

The main reason is client focus—serving the needs of borrowers and beneficial owners. Fixed income securities play a significant role with today's regulatory environment. Regulation is putting pressure on borrowers' balance sheets, creating the need to trade up the credit curve—from equities to fixed income and from fixed income into cash. Regulation is also requiring that collateral be posted against more types of transactions.

Therefore, both beneficial owners and borrowers can leverage our Hong Kong fixed income capabilities to source the required eligible collateral as they execute their investment strategies.

With our fixed income trading capabilities, borrowers can obtain in-time inventory offers and pricing and can borrow and execute the trade in region which helps create a more efficient and cost effective trading environment. For beneficial owners, more efficient trading can help increase volumes and drive more potential opportunities for enhancing revenue.

Borrowers in the Asia Pacific have since increased their demand for fixed income securities. At first, this demand was in the form of flow trading, the answering of day to day queries about bonds that the borrowers might need. Then demand moved on to more structured trading and eventually led to sizable financing deals.

How have our Asia Pacific borrowers and beneficial owners responded to our Hong Kong fixed income capability? The response has been positive. There has been a steady stream of trades and a growing book of business. Term trades are increasing in size and locking in revenues. The number of borrowers with which we trade locally in the Asia Pacific has also expanded. Overall, we can offer more assets in the region and the increase in balances and greater diversity of borrowers helps to create an even more robust agency lending programme for our clients. **SLT**

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"There has been a steady stream of trades and a growing book of business"

Paul Solway, Regional head of securities finance, APAC, BNY Mellon

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Connecting the assets

Regulation has pushed Clearstream into the forefront by virtue of the fact that regulation demands the segregation of collateral, says Charlie Bedford-Forde

What is the ethos behind the Global Liquidity Hub?

The ethos behind the Global Liquidity Hub was to provide our clients with a single global collateral pool. It allows securities to be used to cover securities lending transactions and repo, along with other collateral management functions, without having to re-align securities across borders.

The Global Liquidity Hub's open architecture enables market participants to connect to our collateral management system. It involves for example a partnership with Citibank, BNP Paribas Securities Services and Deutsche Bank in a number of Western European markets, and Standard Chartered Bank in Singapore. The system allows for the use of their domestically held custody positions with triparty agents in Clearstream's Global Liquidity Hub.

That flexibility was created in response to regulatory demands. As more counterparties look at Basel III and its impact on capital, they are beginning to realise that they need to mobilise as much inventory as possible. While Clearstream allows them to mobilise assets they already hold with us, the Global Liquidity Hub allows access to assets held with other domestic sub-custodians. Users can retain those custodian relationships while allowing those assets to be mobilised as part of a book entry transfer process within the custodian, but also make them visible within Clearstream. The assets remain local but their owners are able to get international financing to them.

Regulation has pushed Clearstream into the forefront by virtue of the fact regulation demands the segregation of collateral. The Liquidity Hub will cater to a lot of these needs.

How do all of Deutsche Börse Group's subsidiaries work together within the Global Liquidity Hub?

It very much depends on the circumstances, which speaks to the flexibility of our solutions and the level of customisation that can be delivered for clients. A good example was the decision to combine Clearstream, Eurex Repo and Eurex Clearing's agency lending services to enhance the group's overall securities lending capabilities. The combined service offers customers greater capital efficiency and straight-through processing. Each player performs an essential function. Clearstream manages the transaction as the agent lender and triparty collateral agent, via the Liquidity Hub. Eurex Repo's SecLend market manages the trading venue through its GC Pooling client base, while Eurex Clearing provides clearing services as the central counterparty (CCP) to both sides of the transaction.

We also expect to see more cooperation with other Deutsche Börse companies soon. 360T, a foreign exchange platform, was recently acquired and Clearstream has an exclusive relationship to provide its corporate clients with triparty repo. With the advent of the European Market Infrastructure Regulation, more corporates are likely to want to raise collateral through repo to cover their counterparty needs.

Deutsche Börse Group's securities financing offering is extensive—isn't there a chance that clients could be overwhelmed?

You can't force solutions on clients. We try to present our advantages as individual companies but also highlight the extended benefits of the group. Again, the direction that regulation has taken will make this feature more attractive. At the same time, budgets are tight and people are looking at where they can make wholesale changes to streamline relatively cheaply and we offer that possibility.

What advantages do your European and Asian partners offer?

Our decision to partner with BNP Paribas Securities Services, Citi and Deutsche Bank was driven by client demand. These are local custodians that are strong in equity custody in Europe, so being able to offer mutual clients the ability to finance fixed income and equity held with us locally made a lot of sense.

We chose Standard Chartered in Asia for a similar reasons, as it's actually Clearstream's sub-custodian for a lot of the Asian markets. We saw a lot of opportunities in Asia where Standard Chartered's presence could complement our service offering. In Singapore, for example, we see an opportunity to mobilise more Singapore government bonds internationally.

Do you have a presence in other regions of the world?

If you look at South Africa as an example, the reason we have partnered with Strate is because they have specific needs to manage collateral onshore as part of the domestic solution. A lot of South African banks are unable to invest rand offshore because of the tax implications. Therefore, the ability for Strate to use our technology within the domestic market gives us another arrow in our quiver.

What future opportunities do you foresee with this initiative?

We are looking to engage the buy-side and non-financial entities in this collateral management initiative. Historically, many have just used cash and have no experience in mobilising assets.

We are working with technology vendors and custodians to make sure we can offer a solution that is not only applicable to the wholesale clients that have used us for years, but is also simple and provides the security for those new counterparties that are now going to start looking at collateral for the first time. **SLT**

Charlie Bedford-Forde
Vice president, global securities financing sales and broker-dealer relations
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Rumours and reputation, fact and fiction

‘Shady’ short sellers also identify wrongdoing in other industries, says David Lewis, senior vice president at FIS Astec Analytics

Moody’s released a report on 22 March that made for chilling reading. According to the report, between 2011 and 2015, litigation and conduct provisions consumed, on average, about one-third of pre-tax income for the UK’s five biggest banks. Payment protection insurance (PPI) claims made up a large proportion of this—£33 billion over the same four-year period—and according to Moody’s, this will hit £55 billion when all the largest lenders are included.

Banking as an industry, both in the retail space and investment arenas, has certainly suffered in the reputation stakes in recent times, especially following the financial crisis, and such damage inevitably finds its way to the bottom line. Despite the efforts of many, both within and outside our industry, securities finance and its dependent cousin, short selling, remain firmly on the naughty step as far as the wider public are concerned.

Only recently, in a business meeting, a non-securities finance professional described our business as “naughty”, despite being a seasoned and educated banker themselves. The explanation was that it was somehow distasteful to make money on a falling share price, which is a common refrain among detractors. The argument that searching out over-valued shares that inappropriately attract investor’s capital moved the opinion a little, but such feelings do remain across the spectrum, from public observers to professionals.

However, on occasion, it is the short sellers who identify wrongdoing in other industries. Accusations of false accounting, money laundering and worse can surface in any sector. Let’s Gowex SA was, for 10 years, one of Spain’s most celebrated tech start-ups and was “worth” $2 billion when Gotham City Research exposed the extent of the fraud and false accounting in 2014. Two days after the report was released, €870 million was wiped from the company’s value and, within days, a full confession from the chief executive brought the company down.

This year we have seen a similar story with Wirecard of Germany, a payments processing company. Zatarra Research released a report on 24 February that caused an immediate 25 percent drop in the share price of Wirecard. What has followed is a media storm with two entrenched and diametrically opposed sides. The Zatarra report alleges money laundering including the processing of payments arising from online gambling into the US, where such practices are illegal. For its part, Wirecard, as an element of a robust defence, points out that these are allegations dating from 2010 when they were successfully disproved. Wirecard shares recovered a little as the defence strategy gained momentum, but have since continued to slide. Since the launch of the Zatarra report, the shares have fallen some 25 percent (€42 to €31 approximately) wiping more than €1 billion off their market value.

Part of the Wirecard strategy is to describe the research firm, Zatarra, as “short sellers”. The same description has been levied at similar organisations such as Gotham Research and Muddy Waters, which have certainly not shied away from stating that they were indeed holding short positions in the securities they were targeting. There is little better evidence of an analyst’s conviction than putting their own money where their recommendations lie, but in the same way that shares can be talked up, they can also be talked down.

Figure 1 shows the securities lending volume in Wirecard, taken here as a proxy for short selling. While individual position holders cannot be identified, there is clearly a significant jump in short interest in Wirecard months before the 24 February report was released. Volume more than doubled during November 2015 and has remained relatively constant since.

A number of inferences could be drawn from this evidence. For example, if the November jump in short positions is to be attributed to Zatarra preparing for its attack on Wirecard, this previously unknown group would need the resources to sustain a short position worth approximately €400 million for more than five months. The borrow volume has not decreased, suggesting that, if this was some kind of flash crash raid, the associated short positions have not been closed yet.

Figure 1 also shows that the utilisation levels closely track the borrow volume, indicating that there is little change in institutional ownership of Wirecard. When scandal looms, institutions can often be the first to exit affected investments.

Finally, as is shown by the fee levels now being charged to borrow this share (see Figure 1), this has become one of the hottest stocks in Europe. Keeping positions open that demand high fees requires conviction of purpose. Wirecard has launched a robust response to the allegations levied against it, including the threat of legal action against Zatarra, but time will tell who is right and who is wrong in this case. Both sides have, it appears, very strong convictions and claim to have right on their side giving this battle a truly Batman versus Superman flavour. Pick your side. **SLT**

Figure 1: Borrow volume, utilisation and borrow fee for Wirecard

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Industry **Events**

5th Annual Collateral Management Forum

Date: 02-03 June
Location: Amsterdam
www.glceurope.com

The ongoing flow of regulatory changes created many challenges for financial institutions to ensure that their effectiveness, workflows and optimised operations in the field of collateral management.

The ever changing environment has set many obstacles also in optimising the collateral that is fundamental in order to find a solution to the gap between collateral supply and demand.

Topics that will be covered at the conference include regulatory mandates, digitisation in collateral management and more.

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SLT SECURITIESLENDINGTIMES

Securities Finance Regulation 2016

Date: 18 May 2016 | Location: London, UK

Cost £900 p.p. plus VAT

SLT in association with Consolo Ltd will be putting on this one day event which is designed as a crash course in all the regulatory initiatives in progress that may have a direct impact on securities lending.

The agenda will include the following initiatives, although others may be included as the regulatory environment continues to evolve:

- Securities Finance Transaction Regulation
- CSDR and T2S
- Resolution stays
- UCITS V
- CASS
- EMIR
- Taxation
- Basel III
- CMU

Whilst this list is not exhaustive, it should be noted that these regulations are in development phases and not yet finalised. The presentation will provide up to date status reports for each regulatory initiative.

Attendees: This is intended for anyone directly or indirectly involved in securities financing.
Facilitator: Sarah Nicholson, Consolo Ltd
To register: Email Justin Lawson - justinlawson@securitieslendingtimes.com

CONSololtd

Comings and goings at DNB Bank, Commerzbank and more

DNB Bank's head of trading securities finance, **Dag Rudiløkken**, is set to move to Nordea Bank.

Rudiløkken has served as the bank's senior vice president in the securities finance department since 2003.

Previously, he worked as head of securities finance at DNB ASA, Norway's largest financial services group, of which DNB Bank is a subsidiary, between 2003 and 2006, before moving to Carnegie Investment Bank in Norway as branch manager.

It's unconfirmed when Rudiløkken will move to Sweden's Nordea Bank.

Commerzbank's **Eugene Stanfield**, head of derivatives execution and clearing, is set to leave the bank after eight years.

Stanfield has managed the bank's over-the-counter client clearing, foreign exchange prime brokerage and futures and options execution and clearing since 2009.

Previously, Stanfield worked at Dresdner Kleinwort Wasserstein until 2008, when the British-based investment bank was bought by Commerzbank.

Commerzbank declined to comment on the departure.

Adam Wagner, COO of Blue Jay Capital Management, has been voted to become a director on the California Hedge Fund Association (CHFA) board of directors.

"The key to the long term success of CHFA has been the continual addition of talented, committed individuals to our board of directors and in this tradition we welcome Adam Wagner as our newest board member," said Jason Gerlach, CHFA president, and CEO and managing partner of Sunrise Capital Partners.

"The knowledge and depth of experience he brings to our organization is tremendous and California's alternative investment community will be well-represented by his involvement."

Prior to joining Blue Jay in 2013, **Adam Wagner** was a vice president at Pershing

In his role at Blue Jay Wagner is responsible for the daily trading operations, marketing and investor relations functions at Blue Jay, which manages long/short equity healthcare portfolios.

Prior to joining Blue Jay in 2013, Wagner was a vice president at Pershing, a BNY Mellon company, where he was a senior member of the sales and relationship management group within Pershing Prime Services.

Jerra Stead, IHS chairman and CEO, is set to become chair and CEO of the soon to be created IHS Markit, following confirmation of the merger in H2 2016.

Lance Uggla, current Markit chairman and CEO, will be president and a member of the board of directors.

He has also agreed to take on the role of chair and CEO upon Stead's retirement on 31 December 2017.

The combined company will be headquartered in London, but with key operations remaining in Englewood, Colorado. The deal has already been unanimously approved by the board of directors of both companies and is expected to be completed in the second half of 2016, following shareholder approval.

The remaining board positions will be comprised of 11 members, with IHS designating six members and Markit five members, chosen from their current boards.

Markit and IHS shareholders will own approximately 43 percent and 57 percent respectively on a fully diluted basis.

IHS Markit has already pledged to $2 billion of share repurchases over 2017 and 2018. **SLT**

SLT SecuritiesLendingTimes

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