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J.P. Morgan offers securities lending services in Malaysia

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J.P. Morgan Worldwide Securities Services has rolled out its securities lending capabilities in Malaysia.

It is the first international lender in the Malaysian market to offer a securities lending product, according to J.P Morgan.

Barry Griffin, the head of securities lending trading, Asia Pacific, at J.P. Morgan Worldwide Securities Services, said via email: "From a strategic perspective, we're always looking to further extend our securities lending capabilities into new markets, new sectors and new asset classes. In Asia Pacific, we have a tremendous securities lending platform that has been instrumental in our broader asset servicing build out across the region."

"In this instance, we launched our Malaysia platform as the result of market changes enabling easier access to offshore participants and we expect that as Malaysia continues to grow and evolve, we'll see additional demand for securities lending services in this important market."

He added that J.P. Morgan's global securities lending platform is "regarded as one of the best in the world and in Asia Pacific, so I think it's fantastic that we now have an additional service to provide to our institutional clients".

J.P. Morgan now offers securities lending solutions to major prime brokers and clients with Malaysian assets.

Its customised solutions allow lenders to define their own structures to meet their risk/reward requirements, and its comprehensive indemnification programme against borrower default allows lenders to mitigate counterparty risk across their programmes, according to J.P. Morgan.

read**more** **p3**

SLT IN BRIEF

Moody's downgrades 15 banks

A long wait for Moody's predicted downgrade of 15 banks came late on the 21 June, after the US markets shut.

read**more** **p3**

EquiLend enters data business

Securities finance trading and post-trade services provider EquiLend is introducing a new market data provider for the global securities finance market.

read**more** **p3**

J.P. Morgan offers securities lending services in Malaysia

Continued from page 1

Griffin said: "J.P. Morgan's indemnification is regarded as one of the most holistic and robust in the world. However, we see this as being a much broader product differentiator—it's not specifically confined to Malaysia alone."

Shaun Parkes, the CEO of Asia (excluding-Japan) and Australia at J.P. Morgan Worldwide Securities Services, said: "The future for securities lending in Asia Pacific continues to demonstrate significant potential. Malaysia represents an important part of our regional growth strategy, and is a key value-add for our institutional client base that is looking to diversify their investments and mitigate their risk."

EquiLend enters data business

Continued from page 1

EquiLend said that the data provider, which has almost completed its beta testing phase, will be called DataLend.

The DataLend service will go live later in 2012.

Brian Lamb, the CEO of EquiLend, said: "We are thrilled to bring DataLend to the securities finance market and thus far it has been received with much enthusiasm by its users. We expect DataLend to be embraced by the market as it tailors its high quality data and customises it to our clients' needs."

Moody's downgrades 15 banks

Continued from page 1

But the downgrades did not seem to have a great effect, with the global economy and manufacturing output in China remaining the major worries.

German, French and Italian markets were all down, with the main index down 55 points, and China recorded an eighth consecutive drop in manufacturing output.

After chief executive James Gorman lobbied hard to avoid a three-notch downgrade of Morgan Stanley that the rating agency had threatened, its long-term credit rating was cut from "A2" to "Baa1", three notches above "junk".

HSBC expected a two-notch downgrade but received just one, sending shares down 0.5p to 559p. Barclays was down two notches, and Lloyds was down one, with shares up 0.05p at 31.25p.

RBS was down 1.6p to 242p after its one notch downgrade, which the bank disagreed with.

It stated: "The group disagrees with Moody's ratings change which the group feels is backward-looking and does not give adequate credit for the substantial improvements the group has made to its balance sheet, funding and risk profile. Nonetheless, the group believes the impacts of this downgrade are manageable, bearing in mind its £153 billion liquidity portfolio."

An industry expert said that the downgrades could limit banks' activities, as they will have to increase the collateral in their transactions with each other. The expert added that the downgrades are a constraint on capital and business.

The credit downgrading is indicative of the challenging conditions facing investment banking, with the downgrades placing increasing pressure on how banks source and deploy collateral, said Jonathan Philp, a specialist in OTC clearing and collateral management at Rule Financial.

"A deteriorating credit rating has the pro-cyclical effect of raising banks' cost of funds and eroding profitability, in particular where the institutions concerned have a high dependency on the repo and securities financing markets. Weakening credit ratings also feed into the counterparty credit risk process, resulting in incremental margin calls; essentially, a downgraded bank will be required to provide a greater amount of collateral to support a given level of business activity.

"The credit downgrades therefore place even greater pressure on the processes by which banks source and deploy collateral. Against a backdrop of fundamental post-crisis regulatory change, which emphasises capital and collateral as the financial firebreaks that will prevent future systemic crises, many large banks are already investing in more sophisticated and proactive approaches to enterprise collateral management."

"The clearing houses that are at the heart of the reformed OTC derivatives market structure are setting extremely conservative collateral eligibility parameters, driving demand for a narrow universe of highly liquid assets—assets that are already intensively used in the secured lending markets for funding and liquidity management purposes."

J.P. Morgan has new option for managing collateral

J.P. Morgan Worldwide Securities Services's triparty offering for Chicago Mercantile Exchange's (CME's) IEF4 programme will begin supporting corporate bonds.

The change comes in conjunction with CME Clearing's decision to expand eligible collateral to include corporate bonds.

"Expanding our collateral program allows us to continue to meet the needs of our very diverse customer base, particularly as we approach the new regulatory realities that require more collateral from market participants," said Kim Taylor, president at CME Clearing.

"We have worked closely with both buy-side and sell-side market participants to develop enhancements that reflect prudent risk management as well as provide more flexibility as they transition to OTC clearing."

Qatar 'introduces' sec lending

It has been reported that the Qatar Financial Market Authority (QFMA) has issued new regulations that will enable securities to be lent and borrowed in Qatar.

In the first phase, the new regulations would allow licensed financial service providers to lend and borrow listed securities to settle failed transactions.

Nasser Ahmed al-Shaibi, the CEO of QFMA, said that the regulations are the result of a study of Qatar's capital markets and will help to improve their efficiency, performance and depth, and increase their liquidity levels, according to reports.

US SEC accuses businessman of stock lending fraud

The US SEC has accused Manuel Bello of running an illegal stock lending scheme that netted him $3.2 million.

The New Jersey businessman had two firms, Ayuda Equity Funding and AmeriFund Capital Holdings, which made loans to affiliates of public companies that put up shares of stock as collateral.

The size of the loans were based on a percentage of the value of the stock that was put

up as collateral, generally in the range of 40 percent to 75 percent, US SEC officials wrote in a complaint.

In exchange, borrowers transferred ownership of their stock and made quarterly interest payments over the term of the loan, which typically were three to five years.

Bello and his firms allegedly claimed that they would not sell the stock except in the event of default, and would return the collateral once the loan was repaid.

But Bello and his firms sold the stock once the transfer was made, the US SEC said. In at least 35 instances, he and his firms sold restricted shares without proper registrations, the agency added.

Bello and the firms settled the case without admitting or denying wrongdoing by agreeing to repay the $3.2 million in illicit gains plus interest. Bello also agreed to a $500,000 penalty and a bar from the securities industry.

Omgeo addresses collateral management issues

Omgeo has released new functionality on Omgeo ProtoColl, its automated collateral management solution.

The new version of ProtoColl has been developed with the hope of helping market participants to manage their collateral and risk management operations ahead of the implementation of complex regulatory requirements for OTC derivatives clearing.

Ted Leveroni, executive director of derivatives strategy and external relations at Omgeo, stated: "We are seeing increased focus on automated collateral solutions as firms recognise that they need to act now to prepare their internal processes ahead of the implementation of new regulatory mandates including Dodd-Frank and EMIR."

"While the regulations are still to be finalised, there will always be the need for both bilateral and centrally cleared capabilities and ProtoColl gives clients the ability to manage both from a single platform today."

Calypso links with AcadiaSoft to enrich collateral management

Calypso Technology will integrate AcadiaSoft's MarginSphere service, an electronic messaging and workflow solution for OTC collateral, with the Calypso system.

The partnership combines AcadiaSoft's automation of the margin process with Calypso's collateral management solution.

AcadiaSoft's MarginSphere is a messaging framework for collateral, providing an ISDA-compliant workflow that aims to eliminate dependency on email, phone, fax and traditional communication modes with an electronic interface that provides scalability, security and audit trails.

The Calypso system provides a cross-asset collateral management solution that is integrated with front-to-back office management of OTC derivatives and treasury products.

Under the G20 mandate, required clearing of OTC derivatives is expected to ratchet up global collateral requirements by as much as $2 trillion.

"One margin call typically generates five or more messages, and dramatically more if there are disputes. Given the number of accounts, counterparties and trades that any firm has to maintain, the volume of margin messages can rapidly escalate, creating the potential for errors and large processing inefficiencies," said Chris Walsh, the COO at AcadiaSoft.

HKMA signs collateral agreements with Euroclear and J.P Morgan

The Hong Kong Monetary Authority (HKMA) has signed bilateral agreements with Euroclear Bank and J.P. Morgan Worldwide Securities Services to cooperate in delivering a cross-border collateral management service.

Peter Pang, the deputy chief executive of the HKMA, Olivier Grimonpont, the general manager and regional head of Asia-Pacific at Euroclear Bank, and Kirit Bhatia, a managing director and the head of technical sales in Asia (excluding Japan) at J.P. Morgan, signed the agreements on 20 June.

The new service enables international financial institutions to use securities that are held with Euroclear Bank or J.P. Morgan as collateral in triparty repo transactions with members of HKMA's central moneymarkets unit, so that they can access liquidity from Hong Kong, particularly the Hong Kong dollar and offshore renminbi.

Euroclear Bank or J.P. Morgan will act as triparty collateral management agents to the repo transactions, ensuring that administrative obligations, such as collateral valuations, eligibility, haircuts and substitutions are carried out automatically on behalf of the two counterparties to the securitised deal.

HKMA plans to expand the cross-border collateral management service to allow local financial institutions to use their securities as collateral to obtain foreign currency liquidity, such as the US dollar from international financial institutions in the second half of 2012.

Pang said: "The launch of the cross-border collateral management service is a timely and an effective solution for the market which will provide a solid foundation for the repo market development in future and enhance stability of our financial system. It will also facilitate the expansion of cross-market renminbi funding activities through the cross-border collateral management arrangement, and further strengthen Hong Kong's role as the global hub for offshore renminbi business."

Grimonpont added: "This initiative will no doubt pave the way for other Asian economies to benefit from a similar processing solution. It has taken years of dedicated work at the HKMA and the market as a whole to achieve this accolade."

ECB axes collateral project

The Governing Council of the European Central Bank (ECB) has decided to put the brakes on preparations for the Collateral Central Bank Management (CCBM2) project in its current form.

Significant obstacles were identified in harmonisation, leading to acknowledgment that these needed to be addressed before the project carried on. The existing Correspondent Central Banking Model (CCBM) for cross-border collateral management remains in place.

In the immediate future, the eurosystem will concentrate on implementing the previously announced enhancements to eurosystem collateral management services, namely the removal of the repatriation requirement from the CCBM and the support of cross-border triparty collateral management services within the CCBM.

Both enhancements will be introduced in the eurosystem collateral management framework in the course of 2014. The eurosystem will prepare for the support of T2S auto-collateralisation procedures.

Lombard Risk enhances repo and sec lending modules

Lombard Risk has enhanced its repo and securities lending Colline modules.

Colline is designed for end-to-end, cross-product (bilateral and cleared OTC derivatives, repo and securities lending) collateral management.

John Wisbey, the CEO of Lombard Risk, said: "Firms are increasingly looking to consolidate their margin views and exposure management processes on to a single platform to manage the operational increases emanating from the new regulatory provisions such as Dodd Frank and EMIR."

"The benefits of a single platform to manage collateral include: process efficiency, consolidated statements and reports, regulatory reporting, consolidated inventory management and cross-product collateral optimisation."

Fund enters new credit facility with BNP prime brokerage

RMR Real Estate Income Fund (RIF) has entered into a new $50 million revolving credit facility with BNP Paribas prime brokerage.

The new credit facility bears interest at LIBOR plus 95 basis points and it has a 270-day rolling term that resets daily.

It requires RIF to pledge portfolio securities as collateral up to 250 percent of the loan balance outstanding.

The new credit facility also permits BNP Paribas to lend portfolio securities pledged by RIF up to the loan balance outstanding, and RIF will receive a portion of the revenue earned in connection with lending its portfolio securities.

RIF expects to use the new credit facility to repay amounts outstanding under, and terminate, its existing $10 million revolving credit facility, to fund additional investments, and for additional financial flexibility in managing its investment portfolio.

4sight releases new corporate action modules

4sight Financial Software has developed a new suite of corporate action processing modules for its 4sight Securities Finance and Collateral Management solution.

MXCorner

Evidencing compliance

In the last two issues of SLT, I have talked about the need to implement strategic solutions to ensure that beneficial owners can meet the complex reporting requirements of new regulations. But what about the regulatory requirements that market practitioners will have to meet and not necessarily report on regularly?

The European Council's Short Selling Regulation, which comes into force in November, will require evidence of rule compliance to be retained, rather than regular reporting. Its focus is generally on the entity creating the short sale, and/or the entity from which the security is located (usually a prime broker). However, it is easy for securities lenders to miss the fact that they have to consider their positions too.

In order for a security that is sold when on loan to avoid being classified as creating an uncovered short sale, the lender must "recall the securities so that settlement can be effected when it is due, the exclusion of such cases from the definition of a short sale also involves no risks as regards the timely settlement of the transaction in the concerned financial instruments", according to ESMA. Given that the mechanics of receiving transaction data from sellers (asset manager or beneficial owner) can sometimes mean that agent lenders are not notified of sales until S+1 or even S+2, the agent lender needs to ensure not only robust processes, but evidence of them is retained.

For the majority of loans, recalls settle in time for the sale to settle on the settlement date, but if it doesn't for some reason, can the lender prove to the regulator that the security was in fact recalled in time and that other factors caused the fail? Most lending systems allow you to flag recalls, but once settled, how is this information retained? As the entity responsible for the potential uncovered short sale, a beneficial owner may not want this information regularly reported, but it will want to know that lending agents are retaining sufficient information to prove compliance. This is especially the case when a beneficial owner is prohibited from short selling by its own regulation or stated fund objectives. The likelihood that an odd fail will cause regulators to request evidence is a secondary issue to the need for lenders to ensure that if regulators do ask, the evidence is readily available.

Sarah Nicholson, senior partner
MX Consulting Services

The new modules provide a greater level of automation and workflow processing, with the aim of reducing manual effort and lessening the risk of missed or late claims and processing, according to 4sight.

The modules offer a workflow-based dividend processor for equity cash dividends and fixed income coupon payments for stock loan, repo and collateral transactions.

The system also provides support for non-cash dividends through an array of configurable event types.

Martin Seagroatt, the head of marketing at 4sight, said: "The aim of these new modules is to reduce the number of manual steps and time spent processing events that would previously have led to missed or late claims and processing. The new level of automation and system based processing will provide our clients with greater workflow control, help them to exert less manual effort on corporate actions processing and reduce operational risk."

Canadian mutual fund manager re-signs with Citi

Citi has renewed its agreement with Chou Associates Management and will continue to provide trust and securities lending services for the $600 million that it oversees in mutual fund assets.

Citi will also provide Chou Associates Management with fund accounting, transfer agency and custody services.

Chou Associates Management, which became a Citi client in 2007, has agreed to a five-year deal.

Gurmeet Ahluwalia, the head of Citi's securities and fund services business in Canada, said: "The renewal of this mandate with such a respected market participant is a compliment to the individuals on our team, who work so diligently to ensure our level of service remains unmatched."

"It is also a testament to our bundled investor services offering, which we are able to constantly enhance by leveraging Citi's operations around the world, where we are in more markets than any other competitor."

Fidessa issues new regulation white paper

Trading, investment management and information solutions provider Fidessa has released a white paper that examines the regulatory pressures facing the financial industry in Europe.

The white paper, which is entitled European Regulation—A Tale in Four Acts, aims to help market participants negotiate the increasingly complex web of regulation that will result from the introduction of legislation such as MiFID II, MAD II and EMIR, according to Fidessa.

Fidessa's white paper examines some of the unintended consequences that could result from the proposed regulatory changes and explores how these can be avoided.

"Five years on from MiFID, the regulatory landscape in Europe is now more complex than ever before," said Dr Christian Voigt, a business solutions architect at Fidessa and author of the paper. "Staying ahead of the game has morphed from being a significant challenge to an almost unmanageable burden that is impossible to accommodate without a vast amount of specialist expertise."

Traiana adds brokers to network

Traiana's Harmony CFD equity swap network has added 11 prime brokers for enhanced client servicing for buy-side clients in the past year.

Prime brokers including Barclays, BofA Merrill Lynch, Credit Suisse, Deutsche Bank, J.P. Morgan, Morgan Stanley and UBS are rolling out the solution to their clients.

The total number of CFD equity swap participants on the network now includes 14 prime brokers.

Teresa Heitsenrether, head of European prime brokerage at J.P. Morgan, said: "As our business continues to grow, it was important that we partnered with a firm with the experience and capabilities to provide a world class client servicing solution. With Traianana's extensive network of prime brokers, executing brokers, and buy-side firms, Traiana Harmony was a natural choice."

ECB attempts to increase collateral availability

The Governing Council of the European Central Bank (ECB) will begin accepting a wider range of collateral in its lending operations and assets of a lower quality.

The Governing Council has reduced the rating threshold and amended the eligibility requirements for certain asset-backed securities (ABSs), aiming to broaden the scope of the measures to increase collateral availability, which were introduced on 8 December last year.

In addition to the ABSs that are already eligible for use as collateral in eurosystem operations, the eurosystem will consider auto loan, leasing and consumer finance ABSs, and residential mortgage-backed securities as eligible.

TORA introduces short selling solution

TORA has introduced a reporting solution that is intended to meet new regulatory requirements in Hong Kong that call for short selling positions to be reported.

The new solution aims to enable hedge funds to meet the Hong Kong Securities and Futures Commission's (SFC's) compulsory requirements by consolidating a report of short positions that comply with both the SFC's approved list of equities, which can be shorted, and the newly prescribed reporting thresholds.

The report tool integrates with the TORA Compass execution and order management platform to generate reports on demand or scheduled reports for the weekly or daily requirement set by the SFC.

The new rules from the SFC came into effect on 18 June, with the first reporting day of net short positions on 22 June and a T+2 reporting deadline on 26 June.

Net short positions are then required to be reported weekly with a contingency for the SFC to enforce daily reporting in the event, for example, of a rapid market decline.

OCC issues an interim final lending limit rule

The US Office of the Comptroller of the Currency (OCC) has adopted an interim final rule to amend lending limits for national banks under a requirement of the US Dodd-Frank Act.

From July 21 2012, section 610 of Dodd-Frank revises the statutory definition of loans and extensions of credit for purposes of the lending limit to include certain credit exposures arising from a derivative, securities lending, or securities borrowing transaction, as well as a repo or reverse repo agreement.

The interim final rule implements this statutory change, which applies to both national banks and savings associations. State banks are subject to separate restrictions under section 611 of Dodd-Frank.

National banks and savings associations have until 1 January 2013 to comply with the rule's derivative and securities financing transactions requirements.

Staunton's View

Catching collateral (if you can)

It's difficult to stop harking back to the Lehman Brothers default, but the ramifications of it have had such a penetrating effect on today's business. The most significant impact following the default was the mass (albeit temporary) exodus of lenders from the market. The vast majority of lenders that did suspend lending have been back for some time, but they participate in a much more conservative way than before.

Borrower selection, credit limits and collateral choice have all undergone intense scrutiny and change. The biggest change on the collateral side was that many of those who had previously accepted cash as a form of collateral either no longer wanted it, or those who did limited re-investment into repos to high quality collateral deals. This is understandable when, in nearly all cases, losses in securities lending are attributable to cash collateral re-investment. As a result, agents' cash balances in their re-investment programmes plummeted.

Is now the right time for lenders to return to cash? I think it might be. As of 1 January 2013, under the US Dodd-Frank Act, OTC derivatives for many market participants will have to clear through a regulated exchange and a CCP. If you have traded derivatives before, the concept of posting margin, both initial and variation, will be no surprise, and you can post margin with either cash or certain eligible securities as deemed acceptable by the CCP. This margining of trades is fairly straightforward for the sell side, but for the buy side, which may not have sophisticated collateral management systems and procedures in-house, the task will be more onerous, unless cash is posted.

Where will this cash come from? One easy way to raise the cash is to lend assets out against cash collateral and have the agent lender pass the cash onto the underlying beneficial owner. A few beneficial owners (largely the asset managers) already have these processes in place, but they are taking the cash and investing it into their funds themselves. However, this proposition is slightly different. Raising cash to post as margin to a CCP may be an economic and efficient way of doing it. It's worth a look, and remember; the deadline is looming.

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Keeping it fresh

ISLA's 2012 conference in Madrid had to compete with the European Football Championship for attendees' attention, but the conference's speakers succeeded, tackling some interesting points along the way

MARK DUGDALE REPORTS

Frederick Nadd-Aubert, who heads up global securities lending marketing in the investment banking division of Credit Suisse, asked attendees whether they thought that Greece would leave the eurozone as the country continues to fight economical battles. Sixty percent of those who voted believed that Greece would stay in the eurozone, despite the fact that the country's coalition government was yet to be formed.

The International Organization of Securities Commissions's secretary general David Wright, who worked for the European Commission for more than 34 years, said that the financial crisis, which many blame for the current situation in Europe, did not occur in 2008, but actually happened in August of 2007. He added: "Some thought the regulators would sort it out, but they didn't."

"I don't think Europe can be held responsible, but it is now at the epicentre. The US is more responsible, starting with the subprime crisis."

Wright said that the US's response to the financial crisis has been good, while the EU's response has been found wanting, adding that the EU is a "complicated beast", with its differing political entities and cultures.

Austerity measures have not had the desired effect, but Wright said that he senses that "the EU is moving in the right direction".

Wright went on to discuss 'shadow banking' and what the Financial Stability Board's (FSB's) proposals, which are due out at the end of 2012, will cover.

As one of five main areas, securities lending and repo are high on the FSB's list of shadow banking activities. Wright said: "My advice is the industry should share its ideas [with the FSB]."

He asked attendees to think about how they are going to define the level of transparency that they would be comfortable with to regulators, as well as how they are going to show that there will not be a firesale of collateral in a stress market.

Wright added: "Politicians are not going to wait for perfection. Time is short and of the essence."

In a panel discussion, Tredick McIntire, who oversees Goldman Sachs's agency securities lending business in the US and Europe, said that the first quarter of 2012 was positive for beneficial owners and lenders.

He added that while "prevailing uncertainty has been a break on growth in securities lending", talks between industry members and regulators have been "positive and largely constructive".

McIntire went on to discuss approaching regulatory reforms, including Dodd-Frank and the FSB's work on shadow banking. **SLT**

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Meet Markit Securities Finance

SLT talks to Brad Hunt of Markit Securities Finance about the integration of Data Explorers and offering more to the sec lending industry

MARK DUGDALE REPORTS

What was the motivation behind Markit's acquisition of Data Explorers?

The Data Explorers business, which is now known as Markit Securities Finance, is a fantastic one. It has great people and a track record of innovation. It also achieves something unique in the marketplace; it has a comprehensive dataset covering the majority of the buy and sell sides, which are consumers of and contributors to the data. We were very impressed with the company and we remain impressed with it. Data Explorers is also in a segment of the marketplace where Markit wasn't present before the acquisition. We thought that the Data Explorers business was not only a great asset, but it was important for us to be represented in the securities lending market given the changes going on in the market.

It helps that the Data Explorers business is very complimentary to Markit's existing businesses. This includes Markit's ETF franchise, which covers not only ETFs, but index management and dividends forecasting, as well as Markit's quantitative research business.

What have you been doing since the acquisition in April?

We have focused on the integration of Data Explorers into Markit. The bulk of that is now done in terms of organisational integration. What is very important for Markit is that clients remain unaffected through the transition, which I think has been the case. We have strived to ensure that our clients around the world continue to enjoy the same high level of service as they had before, as well as the attention of the same individuals who serve them. This was very important to Markit.

Has Markit been tempted to change the business in any way?

The approach to integration has been that business should continue as usual. It's a good business and we're not planning on changing anything. From the people to the technology and all of the structures in between, we intend to keep the business as it is. Customers have said that they are happy with things the way they are, so keeping things the way they are is what we want to do.

There are aspects of the Data Explorers business that we looked at and decided to apply throughout the rest of Markit, because the model was so good, such as the account management function of Data Explorers. If you look at Data Explorers very simply, it took something of an obscure dataset—at least in an area where there was a lot of opacity—and it made the data relevant to a lot of different people using a lot of different innovations. These include the delivery and benchmarking capabilities, innovation in rates, as well as the media insights and forums.

What's in the pipeline for Markit Securities Finance?

We're looking to build new products that will solve some of the problems that our clients are facing. A headline theme that is driving a lot of what we are doing is that the securities lending market is undergoing significant change through regulation and the focus on funding. This is affecting the individual cogs, such as collateral, that make the industry tick, because there is an increasing need for transparency and optimisation. We see this as an overriding theme to what we do.

What the team is working on now can be divided into a few different areas. In ETFs, Markit has a significant franchise that can benefit from short interest, supply and demand and rate information. This information is extremely relevant for those who work in securities lending and ETFs, as well as the underlying constituents of an ETF, so it is a fairly quick win to cross-pollinate those two businesses.

We are also looking at ways in which we can provide workflow solutions to those issuing, trading and providing liquidity in the ETF segment. Additionally, the Data Explorers business historically has had success creating optimised tradable indices with providers such as Stoxx and Nasdaq that are based on availability and cost to borrow. That's worked fairly well, and Markit has an indices business. ETFs are really tracking indices and in many ways ETFs are the new passive investment. As they grow, understanding the passive liquidity that's tracking various indices and sub-indices is very important for investors. We're looking at ways to evolve those trading indices and provide some transparency to customers, and there has been some interest in that side.

Markit also has a significant franchise in fixed income data, including pricing and liquidity, on both the cash side and the OTC derivative side. This is really one of the key areas of synergy for Markit and the Data Explorers business—the datasets. Drawing them together is something that we're very focused on.

Fixed income accounts for roughly half of the $13 trillion of global securities in the Data Explorers dataset, of which just under $2 trillion are out on loan. While Data Explorers has built considerable expertise in its equities business, the fixed income data has not been customised to meet clients' workflows, so it hasn't really been monetised in a product sense. As a small company, Data Explorers didn't have sufficient expertise, but with Markit, which has a heritage in fixed income, that has opened up. We're focused on taking the Markit dataset and bringing it together with the Data Explorers dataset to provide additional products for clients. We consider this to be a big opportunity. **SLT**

Brad Hunt
Managing director
Markit Securities Finance

Through the red dust

Can borrowing and lending in Australia step up from a marginalised activity to a significant outlay? SLT finds out

GEORGINA LAVERS REPORTS

When securities lending first grew roots in the 1970s, by way of some fairly relaxed transactions between stock brokers, Australia took note.

In the mid 1980s, the country saw a growing trend in the arena, but it tended to be confined to the margins, due to high borrowing costs. The practice was made up of mostly brokers who were covering failed trade settlements, with the big lenders being nominee arms of major trading banks, which accessed securities from their domestic and international custody clients.

A feature of Australian markets is that they have developed in a balanced way, with foreign exchange, fixed interest, money and equity markets all increasing at broadly similar rates over the period.

As the late 1980s saw the Australian stock market take off, securities lending volumes grew. The only hindrances were two pieces of tax legislation.

The capital gains tax legislation (CGT) of 1985 deemed security loans to be effective disposals for CGT purposes, causing many taxable lenders to bring their activities to an abrupt halt. Superannuation funds lucky enough to be tax exempt continued to supply the market until they themselves became taxable in May 1988.

With these changes, failed trade borrowing, which was so popular among brokers, diminished, while larger arbitrage driven borrowing was sourced offshore.

Consequently, as the handiness of offshore securities increased, there was considerable downward pressure on rates. Overseas lenders who were historically used to lower returns in their markets were prepared to undertake Australian lending for lower fees than the domestic lenders had been. Reforms made in 1989 and 1991 sought to ease the competitive disadvantages of domestic lenders.

Realisation of T+5 settlement in 1992 saw lending volumes fall, as domestic and offshore market participants became familiar with its administration, and failed trade volumes decreased.

However, the securities lending and borrowing operations of most market participants were originally part of their administration areas. As staff matured in the field, and the market became more complex, securities lending desks became distinct departments of their own right.

The rise in market activity has been accompanied and underpinned by improvements in market infrastructure. With Australia adopting the Basel capital framework for banks early on, the country's settlement systems—Austraclear, RITS and CHESS—comply with the highest international standards and Australia's RTGS system is among the best, with a very high coverage of wholesale transactions and integration of securities and funds flows.

Most recently, Australian securities lending has experienced a lull in activity. Trevor Amoils, the desk head of Asia Pacific trading at RBC Dexia Investor Services, provided some insight in the company's 2011 report. He stated: "General flow in Australia continued to be stagnant. Many companies, unfortunately, cancelled the discount on their DRIP programs which impacted revenues on those opportunities. QBE was the standout with a 2.5 percent discount."

"The cash and stock deal that attracted some interest was Newcrest's takeover of Lihir, resulting in demand for the acquirer, Newcrest. Private placements in Karoon Gas, Ampella Mining and Gryphon Minerals drove short-term demand for these names."

What, if anything, has changed in the last year? Carolyn Mitchem, managing director and co-head of global Asian equity finance at BMO Capital Markets, Stewart Cowan, executive director and head of financing and markets products at J.P. Morgan Worldwide Securities Services, Australia, New Zealand and Japan, and Giselle Awad, senior vice president at eSecLending, share their thoughts on the potential of this market.

How would you describe the securities lending market in Australia?

Carolyn Mitchem: We have noticed quite seismic changes in the securities borrowing and lending (SBL) market in Australia in the past few years since the crisis. Along with a more pronounced move towards and an increased growth in synthetic access products (as opposed to the more traditional stock borrow and loan), the regulatory landscape has undergone quite dramatic changes as well. Regulatory amendments around short selling (shorts may only be undertaken on a covered borrow basis) have had a major impact on the way brokers (particularly executing brokers) transact their business. New systems and procedures have had to be put into place to help to facilitate the new SBL regulatory requirements, including enhanced reporting obligations highlighting SBL trades passing through the clearing system. This has all added further layers of complexity to the SBL environment when compared to the pre-crisis landscape.

Stewart Cowan: We have seen some early signs that demand is returning for Australian equities. However, it is still well below 2008 levels. In contrast, demand for Australian Government Bonds remains firm. There is limited supply in the repo market and we have no trouble utilising supply. Demand is being driven by Basel III tier one capital ratio requirements.

Giselle Awad: In terms of participates, there is a proliferation of providers with a local presence, from both the lender and borrower side. In more recent years, we have also seen an increase in third party programmes being offered by both third party specialists and custodians, though the concepts of unbundling and utilising multi-providers are still gaining momentum. In terms of trade flow, demand for Australian equities is relatively subdued. However, focus on the fixed income and repo space is occurring, which is being driven by both regulatory changes and economic forces.

Is the Australian compulsory superannuation scheme still the most active fund in the market?

Cowan: There is a mix of local lenders. The superannuation funds continue to be a major supplier to the market and we expect that this will continue as funds consolidate and grow organically due to the government's mandated and increasing contributions (moving from 9 to 12 percent)

Awad: The Australian pension market is the fourth largest in the world. Funds under management are approximately A$1.3 trillion, with a forecast to grow at 10 percent per year. Additionally, compulsory superannuation contributions will be moving up from 9 percent to 12 percent progressively during the next seven years. Naturally, this means that Australian lenders are predominately from the superannuation sector, but we are seeing increased dialogue with fund managers and insurance firms.

Mitchem: The Australian compulsory superannuation scheme cannot be viewed holistically as just one fund. Employees in Australia have a choice of which funds their superannuation contributions are deployed for management. There are approximately 500,000 super funds available in Australia and this has led to a very competitive marketplace for the management of funds. However, only 300 to 400 funds handle assets totalling greater than A$50 million. The Australian government has also set up the Australian Government Fund in conjunction with this. The purpose of this fund is to meet future obligations for the payment of superannuation to retired civil servants from the Australian public sector.

Do you fear over-regulation?

Mitchem: The increase in tighter regulation has now been in place in Australia for a number of years, so we envisage no immediate change to current policy. There was a marked effect, however, upon introduction during the financial crisis and we saw a very noticeable drop in activity, coupled with a real drawback of funds/clients (beneficial owners) from lending programmes. There was palpable fear from this section of the market and this fed down into many areas of the SBL landscape.

Once clients, and also by extension to a varying degree the regulators, began to get our (the Australian Securities Lending Association and SBL market participants) message and grasp a better understanding of the changes and how to best negotiate them, we noticed a slow and steady return to the marketplace of some of the participants who had initially exited.

We certainly feel that, when looking at the beneficial owners perspective, they feel a much greater degree of comfort and certainty than they did a couple of years ago. However, there still remains a general market-wide feeling of caution, which is in large part a response to the quite severe reaction of regulators to events in the recent past. This may take several more years to remedy.

Cowan: The Australian lending market has had its fair share of regulations to deal with since 2008, when a total short selling ban was replaced with a naked short selling ban, and both short sell and loan reporting. As most of the lenders and borrowers are global players, we are keeping a close eye on the global situation.

Awad: The Australian regulator introduced a number of changes throughout 2008 to 2010 to improve the regulatory and disclosure framework surrounding both securities lending and short selling activities in Australia. These reporting and disclosure requirements have now been integrated as part of normal market practices. It is the potential regulatory changes out of the US and Europe that are currently being monitored, as most participants are part of global businesses and therefore they will be affected.

How have choices of collateral types changed in recent years?

Awad: For Australian lenders; not significantly, as both non-cash and cash have been accepted and continue to be. Lenders are always encouraged to have a diversified collateral profile, within their specific risk parameters, as this allows them to take advantage of market opportunities as they occur.

Mitchem: Collateral requirements/usage is a moving target. After 2008, there was a big move to non-cash collateral, as cash became expensive. However, some domestic lenders required prepayment of non-cash collateral prior to borrowing (as opposed to end of day settlement for the day's exposure). There was movement away from these lenders at the time due to restrictions.

More recently, there has been a bigger push for financing of equity longs, mainly having the mechanism in place to be able to turn them into cash quickly, due to regulatory requirements, and in turn, using the resultant cash as collateral.

There has been growth in triparty arrangements, which has helped with collateral usage. However, all arrangements have their own set of parameters, such as from which part of the index are the equity names acceptable. This in itself has relaxed in recent times with a bit more stability in the market. Settlement of trades DVP versus Australian dollars has the least risk for intraday exposure (as stock and cash move together in the clearing system for DVP/RVP trades). When it comes to cash, Australian and US dollars are the preferred choices. US treasuries and G10 debt remain expensive and cumbersome.

Cowan: The introduction of regulations (Basel III, for example) specific to strengthening banks' balance sheets is creating a ripple effect within collateral management. Acceptable collateral is an important dynamic in every loan trade and there has been increased focus on efficiently and flexibly managing collateral for balance sheet purposes.

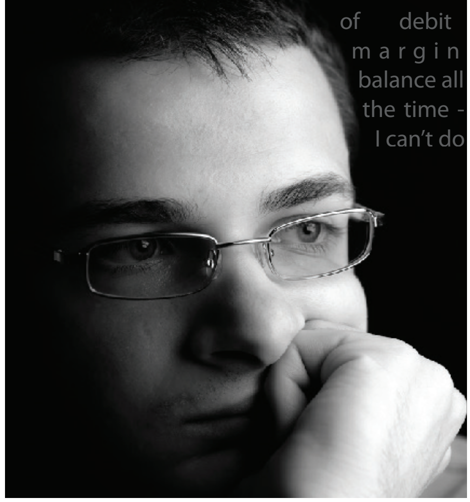
A curious dynamic for collateral is the variance between each financial institution and line of business, depending on internal funding dynamics. These dynamics result in preferred forms of collateral from one borrower to another. As a lender, the greater the collateral options available, the more loan opportunities we can extract on behalf of our clients. Specific to the local market, this means we can accept Australian dollars, government bonds and equities. We also link into global collateral solutions using our global securities collateral management platform.

What are the major obstacles to enhancing returns and how can they be negotiated?

Cowan: As loan demand for Australian equities remains subdued, we have focused on emerging markets (for example, we have just completed our first trade in Malaysia) and working with clients on bespoke trade solutions.

Mitchem: Market demand has just not returned to pre-crisis levels. In part, this is cyclical and understandable. There is not the directional short interest that there once was, as well as a marked effect from the deleveraging of the wider market. We also see traditional index arbitrage participants being predominantly long as opposed to short.

There has been some recovery in mergers and acqusitions and some upside resultant from a slow re-emergence of corporate activity. But this is a slow process. We are also noticing a more crowded group participating in the various Delta One trading strategies, which has tightened spreads considerably in these types of trades. All of this has combined to make the environment a lot more competitive than it once was and we would really hope for some real demand-side growth to aid SBL returns in the future. **SLT**



Platinum shorts

The price of platinum has recovered from its year-to-date low, but the drivers are not a cause for celebration, says Alex Brog of Markit Securities Finance

SHORT DATA

Supply cuts at the industry level have been the main driver for the price recovery, which has outshone gold for the first time in months.

Platinum demand has been supported by buying from consumers, but the malaise afflicting the global car industry and electronics industries has affected its use in catalytic converters, televisions and computer hard drives.

Then there is the popular hedge between the gold and platinum, which some attribute to the latter's resurgence in recent weeks.

Of course not all precious metals are the same, with gold seen as a long-term financial instrument, whereas platinum is an "industrial metal with precious metal qualities", according to ETF Securities, which markets the only US-listed physical platinum ETF, the ETFS Physical Platinum Shares.

Securities lending data shows negligible demand to borrow PPLT, whereas the much larger Spdr Gold Trust has seen the quantity of shares on loan more than double from the annual low recorded in mid-April.

Record shorting of struggling producers

South Africa accounts for 80 percent of the global supply and the country has been accused of keeping a tighter rein on producers than the control exerted by the OPEC (the Organization of the Petroleum Exporting Countries) for oil.

The recent platinum price rally followed news that Aquarius Platinum, the world's fourth largest platinum producer, plans to mothball a mine in South Africa that is jointly owned by Anglo Platinum. This comes hot on the heels of action by fellow miner Eastern Platinum to suspend investment in its Mareesburg mine, according to the *Financial Times*.

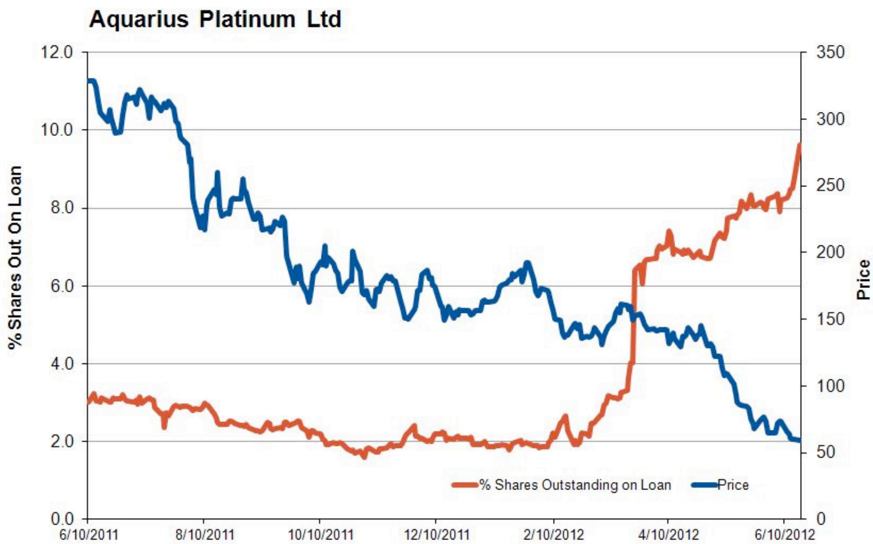
Short interest in Aquarius Platinum reached a high of 10 percent of the total shares while the shares have slipped to a two-year low. Despite this, institutional investor holdings stand at a two-year high, denoting bullish sentiment from the long side of the market.

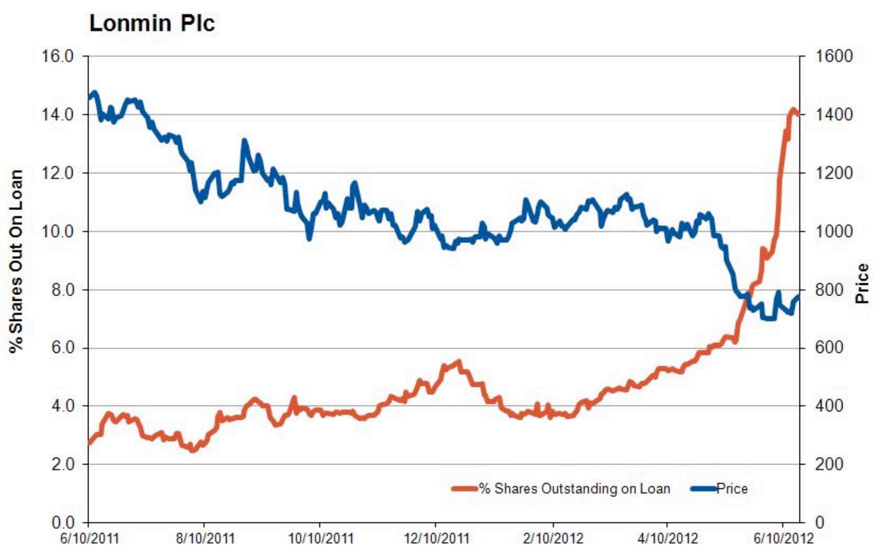
Conversely, international institutional investors who lend their shares have been particularly negative towards fellow South African-listed Eastern Platinum, having halved their holdings over the past year as the share price has continued to plunge. Yet we see little demand to borrow the stock with short interest over this period having been remarkably consistent at only 1 percent of the total shares.

UK-listed Lonmin has seen the most dramatic rise in short interest in recent weeks, with demand to borrow having more than doubled since mid-May to 14 percent of the total shares. This represents two thirds of what can be borrowed from the lending programmes of institutional investors, meaning supply is getting tight and it would be hard to short more of this name.

Short interest surged after the company warned that production stoppages, rising costs and falling prices had affected first half results on 14 May. Negative sentiment had been building in the stock from as early as February of this year.

South African political pressure resulted in Impala Platinum Holdings, the second biggest platinum producer in the world, agreeing to sell more than half of its stake in Zimplats Holdings in March 2012 to government agencies and community organisations. Short interest in Impala has risen to an annual high, but stands at only 1 percent of the total shares. SLT





Industry appointments

Brazilian bank Itaú BBA has recruited **Gregory Wagner** from RBS.

Wagner has joined Itaú BBA as global head of prime services and will be based in New York. He previously worked as global head of equity prime services at RBS.

In his new role, Wagner will take charge of securities lending and collateral trading.

Wagner will report to Christian Egan, who is the global head of equities and prime services at Itaú BBA.

The Brazilian bank is reportedly expanding in the US. It recruited John Cocoran from UBS earlier this year to lead the international bond syndication group in New York. It has also announced new hirings in Brazil, Mexico, Chile and Peru.

Wagner said that he enjoys building businesses and is looking forward to working on Itaú BBA's growth strategy. He added that he is planning to pursue asset management firms, banks, insurers and other institutional investors as clients for the bank, which he said is the biggest securities lender in Brazil.

Amsterdam-based IMC, a prop trading firm, has hired **Wim Den Hartog** as co-head of its Chicago office, a position that will be made effective on 1 September.

Hartog previously worked for the Wall Street firm as managing director of execution and clearing.

The second co-head, **Scott Knudsen**, will be relocated from Hong Kong. Earlier this year, IMC closed its Hong Kong office, with some staff relocating to IMC's Sydney operations.

Michael Johnson has left his role at Penson Worldwide to pursue new opportunities.

Johnson was senior vice president and the global head of pension stock loan at Penson. He oversaw Penson's securities lending business in Dallas, New York and London.

He previously worked as senior vice president of SunGard Securities Finance.

Lionel Guerraz is set to leave the securities lending industry and move into wealth management.

Guerraz currently works as a client relationship management and sales director at UBS in Switzerland.

From 1 August, he will join the UHNW (ultra high net worth) global sales team at UBS to help client advisors with improving their sales across geographic segments.

Andy Krangel of Citi Bank and **James Day** of UBS have been elected as board members of the International Securities Lending Association.

They joined the board in May after elections were held at the end of April.

Day is the head of stock loan trading in the EMEA regions at UBS, as well as its global head of stock lending sales and marketing.

Krangel is a director in Citi's agency securities finance business and is the EMEA head of securities finance product management. He also manages the business's global product development team.

Antoine Babule is the new US head of Newedge.

Babule, who will split his time between the New York and Chicago office, replaces Bill Sexton, who recently left the firm.

The firm is a joint endeavour of Société Générale and Crédit Agricole CIB that offers prime brokerage services to hedge funds.

Babule joined Newedge in 1995, previously holding senior roles including CEO of Newedge Canada.**SLT**

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