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ISSUE009
21.09.2010 TUESDAY

European Beneficial Owners' Securities Lending Summit last night!

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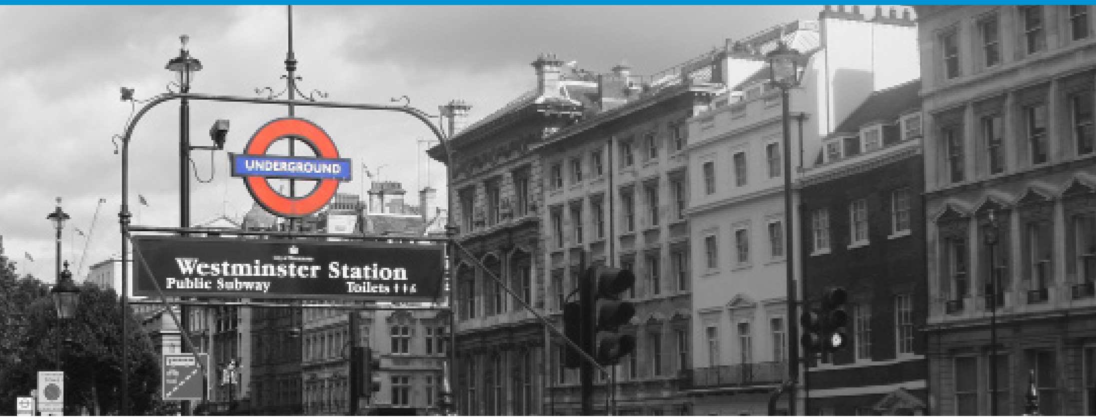

NEWS**IN**BRIEF

SECP approves paper on margin trading

The Securities and Exchange Commission of Pakistan has approved the final concept paper on the proposed leverage product margin trading system.

The paper had been amended following concerns expressed by the chairman of the Karachi Stock Exchange, but was approved by the board chaired by finance secretary Salman Siddique. Speaking to PakTribune, one insider said: "As the concept paper is finalised, the rules for the leverage product would be formulated by the independent committee constituted by the SECP, the very time that prepared the concept paper."

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Data Explorers expands in Asia

Data Explorers, the provider of securities financing data and daily long and short institutional fund flow insight, has opened its office in Hong Kong ahead of the first Asian Securities Financing Forum in Hong Kong on 7th October.

The office will be lead by Karen King, director, Asia with support from Jules Pittam, managing director in London. Emmie Osawa has strengthened the team having joined the company from the securities lending desk at BlackRock in Tokyo.

read**more** **p3**

"Joint response" required on regulation threat

LONDON 21.09.2010

IMN's 15th Anniversary European Beneficial Owner's Securities Lending Summit saw regulation at the top of the agenda, with a call to action from one panellist that all industry participants - from beneficial owners to prime brokers to hedge funds - must play their part in ensuring that any new rules introduced are fair and ensure the industry is able to continue and thrive.

The first day got off to a positive start, as SunGard's Timothy Smith reported that while securities lending had historically been mired in opacity, the new buzzwords were scrutiny and transparency. The opacity, said Smith, was not the result of any malevolent factors, but simply the result of how the market had developed.

The new transparency, and the scrutiny, came as a result of pressure from industry participants, beneficial owners and, of course, regulators. This new outlook, said Smith, is a positive development in the current climate: "2010 sees securities lending at a crossroads. What's going to happen in 2011 we don't know."

The effects of the new regulation remain an issue, however. "We are in a very politicised environment," said Paul Christie, marketing director at Emergent Asset Management, a hedge fund manager specialising in Africa.

"It's to assuage the public's demand for hedge fund managers and others in the industry to be chastised. It's changing the regulation and that's not necessarily going to be for the greater good."

Data Explorers' media director Will Duff Gordon, said that what is needed is a co-ordinated industry response to ensure that the market was not damaged by regulators, highlighting in particular the proposed new reporting requirements for short selling.

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INSIDE SECURITIES**LENDING**TIMES

SECP approves paper on margin trading

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There are still a number of stages to go before the system can be introduced. The formulation of the rules surrounding its usage is expected to take about a month, which then need to be approved by the Commission. Final sign-off will come from the Law Ministry.

"The product cannot be in place before two months, as the Law Ministry would give the final nod," sources in the SECP said.

Trading activity in Karachi has declined in recent months, and the Commission hopes that the introduction of the system will stimulate growth.

Data Explorers expands in Asia

continued from p1

Fluent in Japanese, Emmie will help Data Explorers develop its business in Japan.

The launch of the Data Explorers office in Hong Kong comes as the firm stages the inaugural Asia Securities Financing Forum, which takes place at the Conrad Hotel in Hong Kong on 7th October. Chaired by Steve Sedgwick from CNBC, the agenda features a keynote presentation by Dr. Michael McKenzie on the role of short selling in equity markets. Experienced panellists from the global hedge fund community, institutional lenders, market practitioners as well as representatives from regulators and trade associations will debate the future of securities lending in the region.

Jules Pittam, managing director, Data Explorers commented: "Asia stands out as a region where the income from securities lending is gently rising. We have long term relationships with clients across Asia and Japan who use our daily global content to support their investment decisions and manage risk. We are excited to formalise our presence in the region ahead of our first Securities Financing Forum and are pleased to welcome Emmie Osawa to the team."

ISLA: Short selling disclosure threshold too low

Proposed short selling disclosure regulations announced by the European Commission (EC) are too stringent and threaten market efficiency, according to the International Securities Lending Association (ISLA).

ISLA supports transparency measures that create disclosure symmetries with long positions - including private disclosure to regulators and anonymised reporting of aggregate reported positions - but believes the EC's proposed public disclosure threshold of 0.5 per cent for short sales is too low. "Evidence from prime brokers and market studies show that short selling activity is artificially reduced by investors seeking to avoid short selling above public disclosure thresholds. This undermines market efficiency by reducing liquidity and price discovery, while also widening dealing spreads," said Kevin McNulty, chief executive of ISLA.

"This ultimately results in more expensive and risky investment conditions, while also lowering securities lending volumes and the returns available to long term institutional investors such as pension funds."

While in agreement with the EC's desire to harmonise short selling regulations, ISLA is concerned that a number of its proposals go beyond the framework of the original consultation and are excessive - including for naked short selling, flagging of short sales and for automated settlement buy-ins. A technical matter that also needs to be addressed, is to make clear that an investor who sells shares that are on loan is not deemed to have entered into a short sale.

ISLA also said it believes the proposed EC requirement to locate and reserve shares before all short sales is unnecessary, adding additional costs and processes for little or no benefit. ISLA also believes current conventions for locating shares and determining liquidity work well, and there is no evidence of settlement problems caused by naked short sales.

Flagging short sales - this provision is somewhat surprising as it appeared to have been ruled out during the CESR consultation. ISLA believes that the benefits of flagging short sales do not outweigh the considerable IT costs that firms and trading venues will incur.

Buy-ins - Although ISLA supports the principle of sensible settlement discipline, it believes the EC's proposal for T+4 automated buy-ins are too draconian and will cause a reduction in securities lending activity and market liquidity, as investors hold back excessive quantities of securities to manage this requirement.

European repo market surpasses pre-crisis levels

The European Repo Council of the International Capital Market Association (ICMA) today released the results of its 19th semi-annual survey of the European repo market. The survey sets the baseline figure for market size at EUR 6,979 billion representing an increase of 25 per cent on the figure of EUR 5,582 billion for the previous survey in December 2009. This figure takes the size of the market above the previous highest figure of EUR 6,775 billion recorded in June 2007 before the financial crisis.

The results of the survey confirm the continuing recovery of the European repo market and the underlying trading activity that it supports. The survey is based on returns received from 57 offices of 52 financial groups, mostly banks, including most of the the largest European repo market participants. The aggregate figure for market size masks a very varied picture for participating institutions; some have emerged from the recent financial crisis with unimpaired balance sheets and have been able to exploit their strength in a market where many competitors have been forced to consolidate or even contract, and some have disappeared altogether. These institutions have consequently captured greater market share, as is evident in the growing degree of market concentration, 10 firms in the survey accounted for over 68 per cent of the total repo business, well above the historical norm for the survey, which started in June 2001.

The survey also confirms the broader underlying shift towards greater use of Central Clearing Counterparties (CCPs) for repo business. Until recently, access to CCPs was largely restricted to repo business transacted on electronic trading systems. Over the last two years, however, the post-trade registration of transactions negotiated, not electronically, but directly with other parties or through voice-brokers, has become significant. In the latest survey, post-trade registration of direct or voice-brokered repos through CCPs reached 8.7 per cent, which means that the total share of surveyed repo business (electronic and non-electronic) that was cleared across CCPs was 22.4 per cent.

Chairman of the ICMA European Repo Council, Godfried de Vidts said: "The increasing share of central clearing in the European repo market shouldn't make us complacent. There are unresolved clearing and settlement issues in a number of markets which continue to create difficulties in the settlement of bilateral trades and also for electronically originated as well as centrally cleared trades in certain jurisdictions. The ERC is keen to see further progress in the clearing and settlement area through regulatory initiatives like EMIR, as proposed by the EU Commission, but also through continuous work at the ECB chaired COGESI working group."

Other key findings of the survey include:

The market share of electronic repo trading continued to fall, touching 22.5 per cent compared with 27.5 per cent in December 2009 and a high of 28.5 per cent in June 2009, as the growth in this sector failed to keep pace with the rapid expansion of the overall market. On the other hand, voice-brokers recovered market share, to reach 20.3 per cent from 18.5 per cent.

The market share of both floating-rate and open repos recovered to 10.1 per cent and 6.1 per cent respectively. The share of floating-rate repo traditionally reflects changes in interest rate expectations. Open repos, which are convenient short-term financing tools, were adversely affected by the recent market crisis, so their revival can be interpreted as an indicator of improved confidence.

Major reshuffle at BNP Paribas Securities Services

BNP Paribas Securities Services has reorganised globally, introducing a business-line and regional orientated organisation which reflects the increasingly global needs of its clients and the company itself.

Four global business lines have been created to develop and deliver optimum solutions and operations across the Securities Services network.

Asset and fund services, headed by Philippe Ricard
Clearing and custody services, headed by Alain Pochet
Corporate trust services, headed by Alain Pochet
Market and financing services, headed by Florence Bonnevay

Business line heads will report directly to Patrick Colle, CEO of BNP Paribas Securities Services. A client development team has been created to manage business development by client segment and by region.

The six client segment heads and eight regional managers are under the management of Charles Cock, who reports to Patrick Colle. They will work together in close collaboration with the business lines to define the evolving strategy and product mix for their target clients across multiple markets.

Alternative investment managers, headed by Maria Cantillon
Asset managers, headed by Margaret Harwood-Jones
Asset owners, headed by Dietmar Roessler
Banks, headed by Nadia Diego
Broker-dealers and investment banks, headed by Alan Cameron
Corporates and issuers, headed by Pascal Pommier

Regions
Asia Pacific, headed by Lawrence Au
France and Belgium, headed by Jean-Marc Pasquet
Germany, Northern Europe and CEE, headed by Gerald Noltsch
Italy, Switzerland and Mediterranean Basin, headed by Alessandro Gioffreda
Luxembourg, Dublin and other fund domiciles, headed by Frederic Perard
North America, headed by Christina Feicht
Spain, Portugal and Latin America, headed by Alvaro Camunas
United Kingdom, Middle East and South Africa, headed by James McAleenan

Commenting on the reorganisation, Patrick Colle said: "Our new organisation will mean that we are more closely aligned with our clients' globalising needs and will create greater efficiency and performance across our business. It reinforces our agility and ability to create and deliver innovative solutions. We are fast becoming a truly global player and this reorganisation will help us facilitate our clients' ambitions and accelerate our growth around the world."

ITG Goes Live on SunGard's Stream Phase3 Interface

Investment Technology Group is now using SunGard's Stream Phase3 solution to process institutional equity trades via The Depository Trust & Clearing Corporation's (DTCC's) Institutional Delivery Netting Service (ID Net). SunGard is the first application service provider (ASP) for broker-dealers to offer securities processing support for ID Net, while ITG is the first broker-dealer to use the ID Net service through the Stream Phase3 solution.

ID Net extends the benefits of netting to institutional trade settlement by giving broker-dealers the ability to combine their eligible and affirmed institutional equity transactions with their Continuous Net Settlement (CNS) transactions. This reduces delivery fees and movements to and from accounts, as well as helps to mitigate operational risk and reduce costs across the clearance and settlement process.

A real-time, global multi-asset securities processing solution, Stream Phase3 provides full processing support for ID Net, including real-time functionality to help broker-dealers streamline the clearance and settlement process and reduce exposure. A customer of Stream Phase3 since 2006, ITG began using the system's ID Net processing capability in June 2010.

Stephen Wasserman, director of settlement product management at DTCC, said, "ID Net helps to increase the overall certainty of settlement for matched institutional trades, encourages early affirmation and reduces risk. We're pleased to work with SunGard as the first ASP for broker-dealers to fully support ID Net processing for institutional trades and to help ITG begin realising the risk mitigation and cost reduction benefits of the ID Net service."

Tony Portelli, managing director and head of operations at ITG, said, "The ID Net capability of Stream Phase3 is particularly useful for institutional broker-dealers such as ITG. With products such as Stream Phase3, SunGard helps us efficiently manage high-volume and high-value institutional trade processing while reducing transaction fees and costs."

Gerry Murphy, president of SunGard's brokerage and clearance business, said: "As the volume of institutional trading grows, the number of steps, risks and costs in the overall clearance and settlement process also increases. We continue to adapt to an ever changing industry, and we are pleased to help ITG become an early adopter of the ID Net service and Stream Phase3's ID Net processing."

Direct Access Partners buys EFX

Institutional agency-only brokerage firm has bought EFX Prime Services from First New York Securities.

The EFX Prime Services team will integrate into Direct Access Partners. Brian Stutman will be managing director, Andrew Saunders will head up the capital introduction programme and Geoff Webster will join the prime operations group.

"The addition of the EFX Prime team adds significant expertise, strong client relationships and a successful capital introduction program to our global prime effort," said Ben Chinea, CEO of Direct Access Partners. "Working with our proven capital raising team, Direct Access Partners is optimally positioned to address the entire spectrum of hedge fund clients-including start-ups, emerging funds and established managers."

Deutsche Bank Links to DTCC's Contract Reconciliation Service

The Depository Trust & Clearing Corporation (DTCC) has announced that Deutsche Bank has linked to its Loan/SERV Contract Reconciliation Service, a second generation reconciliation service that will boost efficiencies, reduce errors and help automate the processing of syndicated loans.

DTCC's Contract Reconciliation provides reconcilement for syndicated loans at all levels, from commitment and facility level down to individual contracts with all relevant transaction detail.

DTCC's Loan/SERV is a suite of services that is helping to automate and streamline the processing of syndicated loans. DTCC introduced its earlier Reconciliation Service in 2008, which enabled agent banks and lenders to view and reconcile loans at a total commitment balance level; Contract Reconciliation followed in 2009.

"Contract Reconciliation provides market participants with more than 30 new data fields such as information on interest rates, margin and fee calculation, drawn and unutilised balances, and payment-in-kind balance," said Mathew Keshav Lewis, DTCC vice president, European Loans Product Management.

"One of the major benefits of DTCC's Contract Reconciliation is that it will help lenders and agents like Deutsche Bank correct errors in cash accruals and related cash flows before they become problems. This helps reduce profit and loss adjustments that come with processing errors and eliminates the time and effort required for manual tracking and correcting of these errors," continued Lewis.

Deutsche Bank is one of the eight leading global agent banks using DTCC's reconciliation services. The other banks are: The Bank of New York Mellon, Barclays Capital, Citi, Credit Suisse, Goldman Sachs, J.P. Morgan, and RBS.

Euroclear to settle transactions in the Chinese Yuan Renminbi

Euroclear Bank has announced that clients will be able to settle transactions and deposit Eurobonds and Hong Kong domestic securities denominated in the Chinese Yuan Renminbi in Euroclear Bank, the international central securities depository. The first transactions in Renminbi may be settled on 27 September.

Olivier Grimonpont, regional head and general manager of the Euroclear Bank branch office in Hong Kong, said: "With a consistent presence in Asia since 1987 and a comprehensive operations centre in Hong Kong, Euroclear Bank is ideally positioned to support the booming Renminbi-denominated securities market.

"As offshore borrowers look to raise funding in Renminbi or to broaden their investor base, investors will be able to settle these transactions in Euroclear Bank and eliminate foreign-exchange risk by having to settle in alternative currencies. The steady supply of Renminbi Eurobond issues to date, with ever-increasing sizes and tenors, demonstrates a growing market appetite for these securities.

"Euroclear Bank aims to take an early and significant role in servicing these securities for issuers and investors alike."

According to the People's Bank of China, the volume of global trade settled in Renminbi has grown from 3.6 billion in the first half of 2009 to

70.6 billion in the first half of 2010. The People's Bank of China and the Hong Kong Monetary Authority recently reached an agreement for the offshore Renminbi business to be supported in Hong Kong.

The Yuan Renminbi is the 53rd settlement currency offered by Euroclear Bank.

Securities lending 'does not adversely affect equity values'

New research suggests that fund managers who participate in securities lending programmes do so without 'generating adverse effects on the value of their holdings'.

The report, from the National Bureau of Economic Research, found that fund managers can earn substantial fees without jeopardising their fund's value.

The study was carried out in 2008 and 2009, when the researchers worked with a money manager to make available two-thirds of a high loan fee stock in the portfolio. In total, over USD800 million of stocks were lent.

The study says that while external market conditions will affect the fees for the securities lending, the fact that they were lent did not affect the underlying value of those stocks.

"Our general lack of results on the moments of returns and bid-ask spreads of the stocks whose shares experience an exogenous supply shock suggests that supply restrictions to shorting may not be an important factor for asset pricing," the report explained.

New SL guide for UK pension funds

A group of UK financial trade bodies has published a new guide to securities lending for UK pension funds.

Pension fund trustees have long called for more information on securities lending, while industry participants have expressed concerns that use of securities lending by pension funds will not rise without further education.

Speaking to the Financial Times, Julian Le Fanu, policy adviser for investment regulation and funding at the National Association of Pension Funds, said: "The concerns have been on two issues: first, whether lenders are fully aware of the risks involved, and alongside that, that lenders might not be fully aware of the benefits of stock lending."

The guide, said Le Fanu, is independent and neutral, and points out both the benefits and the risks of getting involved in securities lending. It covers the administrative and operational aspects of the service, and gives a checklist of questions that trustees should ask before embarking on a programme.

It's estimated that around 70 per cent of larger UK pension funds are currently active in securities lending, while smaller funds are more likely to get involved through pooled vehicles.

Australian market bounces back

The Australian securities lending market has now recovered to pre-global financial crisis levels, said Peter Martin, chairman of the Australian Securities Lending Association (ASLA).

Australia was not hit as hard by the world crisis as many other developed economies, but it still did see a significant fall in available equities.

But while demand is still at comparatively low levels, most funds that placed restrictions on their securities lending activities have now removed them.

"Certainly from a supply perspective, it's back to what it has been historically with about $200 billion worth of lendable equities," said Martin.

Integrated Asset Management announces new launch

Integrated Asset Management has announced the launch of River Plate House Capital Management.

River Plate House is a global alternative investment manager offering macro global government bond long / short investment strategies focused on real interest rates, as well as customised solutions for managing asset / liability and longevity risk.

Michael Hyman said "we are in a generation where rising real interest rates will be at the forefront of investors' minds and with the support of IAM, River Plate House is poised to take advantage of opportunities in the global government fixed income markets that have not been available for a long time".

Victor Koloshuk, chairman, president & CEO of IAM, said "The timing of the launch of River Plate House is ideal as pension funds refocus on real rates of return and LDI, and insurance companies seek to contain longevity risk and achieve more effective asset/liability matching."

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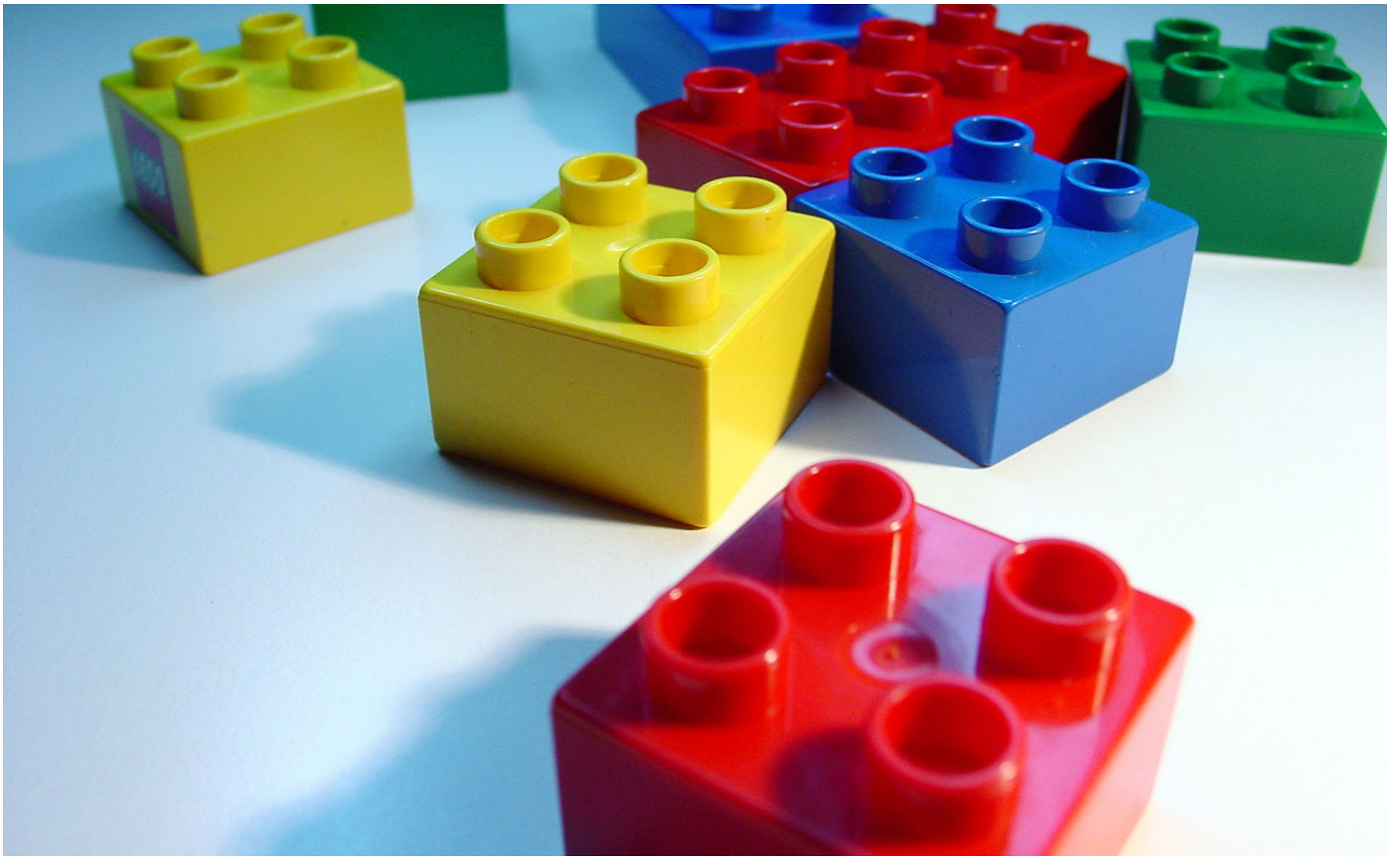

India

It's early days for India's securities lending industry, but the building blocks are in place

BEN WILKIE REPORTS

With an enormous population, a well-educated and committed workforce, and a legal and financial infrastructure that is at least recognisable to major financial institutions, India is set to become a major financial player, and the structure for a booming securities lending market is in place. But it's not quite there yet.

The problem is essentially the same as for anyone who wants to do any kind of business in the country: bureaucracy and inertia. The Indian Government is keen to attract international investment and build up a domestic industry, but when it comes to financial markets it is treading carefully - the economy is by no means as fragile as that of some of its neighbours, but it doesn't want to risk the kinds of problems seen around the world over the past couple of years.

Securities lending and borrowing has actually been available in India for many years. The Securities and Exchange Board of India (SEBI) first permitted transactions as early as 1997, via authorised intermediaries. A range of financial instruments was allowed, including cash, bank guarantees, Government securities, CDs and other registered securities.

> SEBI has relaxed the regulations surrounding securities lending and borrowing

The rules around this introduction were very much geared to the domestic market, however, and weren't really brought in to take securities lending as a financial product in its own right - it was simply to reduce the risk of settlement failures, something that was already in place through other measures, such as daily auctions on the exchanges. But it has moved on.

Over the past few years, SEBI has relaxed the regulations surrounding securities lending and borrowing. Short selling is now allowed, and securities lending tenures were permitted for up to seven days, then 30 days and, since the start of the year, 12 months. Transactions can still only be made in securities that trade in the futures and options segment. The auction process still used to reduce settlement risk, but providers feel that this is an archaic system, and the removal of the process will stimulate the securities lending market.

"Settlement risk is key to securities lending, and we want to have a system that is recognised internationally," says one participant. "But the auction process is holding us back - people who have been in the market for a long time are sticking to what they know and steering clear of


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the more advanced options. If we can get rid of auctions [as has been proposed] then securities lending can only grow."

Vikramaditya, head, HSBC Securities Services (India), in Mumbai says, "Securities lending and borrowing will enable the market to reach the next level in terms of infrastructure, and increase the options available to market players."

Participants

Becoming authorised to participate in securities lending activities is relatively straightforward, even if it can take a long time. Domestic providers and mutual funds are permitted to operate, and international firms are allowed to apply for authorisation. Custodians with a minimum specified net worth may also be considered as an intermediary.

> In percentage terms, growth this year has been fantastic. In real terms, levels are still very low

The main lending and borrowing comes from the large domestic mutual fund arena, and local and international banks. There is some interest from international funds, but this is yet to materialise. There are also calls for insurance companies to be allowed to come into the arena.

"India has a large and growing middle class, and they are increasingly keen on putting their money to work," says one fund manager. "Domestic funds management firms such as Reliance have seen a huge inflow of monies and the fund sector is growing faster than almost anywhere else in the world. As the funds become more comfortable with securities lending, there should be a significant amount of activity."

Growth

In part, the growth is being driven by India's greatest export: talent. Thousands of educated Indians are working for the biggest financial institutions all over the world, and when they return to their home country they have built up new knowledge and enthusiasm about the potential of securities lending. This is then feeding through to the domestic banks and the domestic arms of the international providers, the stock exchanges and the regulators.

"Things always happen slowly in India," says trader Naveen Khalia. "We have the world's worst bureaucracy and - when it comes to Government bodies - a fear of using initiative. "But people who have worked abroad are coming back and saying India is ripe for a booming securities lending industry. It has it all - a growing and untapped fund market, growing electronic trading platforms, a motivated and educated group of professionals who can cope with the business, and a reasonable regulatory environment."

In percentage terms, growth this year has been fantastic. In real terms, levels are still very low. Between January and June this year, there was just one transaction on average every two trading sessions; in July and August it rose to an average of about seven a day, and so far this month it has reached around 15 trades a day.

This has coincided with the implementation of the new rules agreed at the start of the year, and also the increased flexibility in the type of contracts which allows borrowers and lenders to make an early recall or repayment of the securities.

Kapil Seth, head, HSBC Securities Services (India), says, "We haven't seen much activity on the securities lending front. The volumes in the past two months may be from domestic participants taking advantage of arbitrage opportunities between the cash and futures markets. There's nothing to indicate to us a reversal of trend as far as interest from foreign institutional investors goes."

It's generally accepted that it will be foreign investors that drive the market. As securities lending volumes shrank worldwide as a result of the downturn, entering new markets became less important. But as Indian businesses become increasingly global - and many Indian companies are comparable in size to the largest multinationals - more investors are taking an interest.

Some of the world's biggest international banks already have a major footprint in the country, with HSBC seemingly leading the way. And where these behemoths go, others will follow. **SLT**

LATEST NEWS

Data Explorers has launched its insight about short selling activity is now available as a weekly broadcast in Hindi.

DX TV weekly broadcasts in Hindi will be produced each Friday and highlight key short selling insight around the world. This week's broadcast focuses on Asia and highlights short interest activity in some interesting companies.

Jonathan Morris, COO, Data Explorers commented: "With increased market understanding of short selling, we have seen investor demand from all over the world for our short selling insight. We are launching our news in Hindi for the Indian speaking audience around the world. In light of India's strong growth of over eight per cent and unprecedented economic expansion, we believe our broadcasts in Hindi will help foster a greater understanding of global short selling and institutional fund flow activity".

Participants can sign up for the reports at www.dataexplorers.com/hindi

Right of reply

Last issue's CCP Panel debate sponsors give their reactions

The debate in the last issue on the future of central counterparties threw up a wealth of interesting debating points, with a real divide between some beneficial owners and other industry participants.

The sponsors of the debate, SecFinex, Quadriserv and OneChicago, all made their points during the debate. They have now had the opportunity to reflect upon the issues raised, and are able to discuss how the market moves forward.

There seemed to be a difference of opinion about who benefits from a CCP, intermediaries or lenders/borrowers. Because of pricing transparency, the beneficial owners and borrowers clearly benefit at the expense of intermediaries. Lenders and borrowers are able to interact more directly, allowing more of the profits to pass directly to themselves. This free market system also allows price to dictate execution of a loan and not the strength of a relationship with a broker.

Abel Aronovitz, director, institutional sales, OneChicago

With respect to regulatory capital/balance sheet usage not being an issue for agent lender/beneficial owners:

In a world where historical stressed volatilities in equities are in the five per cent to 10 per cent range and SBL collateral rates are 105 per cent there is a risk gap of between five per cent and 15 per cent of the loan amount because you cannot assume that at the point of liquidating collateral and replacing loaned securities, the loan and collateral values will vary in the same direction. If there exists a guarantee to return stock in the event of a default, this is the amount that should be covered by capital.

With respect to the effects of Basel III on the business:

Basel III is just one example of international regulators' determination to move as much OTC business as possible into CCP structures (see: BIS: Group of governors announcement here)

As well as increasing regulatory capital, regulators are also tightening counterparty risk rules and increase collateral haircuts (see BIS: 'Strengthening the resilience of the banking sector' page 45 here.)

The new rules will be ratified in November and enacted by member countries starting in 2011. Minimum capital will rise from 2013 but individual countries may enact transition arrangements earlier.

With respect to the complexity of a CCP in a beneficial owners programme:

The general consensus from the community has been one of a lack of clarity. If the community has fragmented conceptions of the value a CCP brings to the securities lending market how can then they educate their underlying client base. With the recent introduction of the white paper we are hoping the community can formulate its own opinion and begin to discuss opportunities for participation.

Allen Postlethwaite, chief executive officer, SecFinex

The panel convened by *Securities Lending Times* to discuss the role of a CCP model embodied much of the diversity of opinion that has marked the debate at large. We enjoyed being a part of that discussion, and welcome this opportunity to expand on some of the key themes.

As operators of AQS, the world's largest CCP-based securities lending market, we believe that as a preliminary matter – particulars of the larger debate aside – commercial and competitive interests are leading to structural changes in the market.

In our experience, the unmistakable momentum behind the adoption of a CCP model in the securities lending market is being driven by on-the ground, competitive interests. This is a common dynamic after transformative market events, such as we witnessed in 2008-2009, and is an eminently rational response to the inefficiencies and outsized risk profiles that the crisis highlighted. Specifically, we are seeing clear demand from all participants in the securities lending market for:

- Electronic, direct market access that facilitates the shared needs of wholesale lenders and retail borrowers; including the dynamics of supply and demand as well as their common requirements and desires as fiduciaries

- Dealer-sponsored access to a central market that allows the brokerage community to remain in control of both the fair market cost of providing market access as well as their institutional risk management processes

- Capital, margin, balance sheet funding and risk-based efficiencies for the dealer community

A second key point that emerged from the Panel is the utility and relevance of the CCP model for all participants in the securities lending value chain. The Panel spoke with a largely unified voice concerning the benefits borrowers and hedge funds, for which transparency and efficiencies lead to clear competitive advantages. The discussion concerning benefits to lenders and beneficial owners was more nuanced, though no less critically important to reforms shaping the industry. Our own experience is again illustrative, as we see the implantation of more rigorous processes and risk management protocols from these market participants since the 2008-2009 financial crisis. More specifically, a fundamental reassessment of the risk and rewards inherent in securities lending programmes has reinvigorated the intrinsic lending model, which argues in favor of a transparent, competitive marketplace with efficient pricing and best execution standards. These attributes are of course at the competitive center of the CCP

Katharine Gill Law, chief marketing officer, Quadriserv

The role of short-selling

In the third part of our series on the ICMA White Paper looking at the European repo market, we look at the benefits and risks associated with short selling

MARKET RESEARCH

Strong demand for a particular security in the repo market, as reflected in special repo rates, is a measure of the need to cover short positions in the "cash" market. A short position is created by the sale of a security in the cash market by a party who does not own that security and borrows rather than immediately buys the security in order to make delivery.

The sequence of establishing and running a short position is as follows:

A party (the short-seller) sells a security which he does not hold in his inventory to another party in the cash market.

In order to fulfil his commitment to deliver the security to his cash market counterparty, the short-seller borrows that security from either the repo market or securities lending market. This borrowing can be done before or after the short sale. The short-seller will use the cash proceeds from the short sale to the cash market to fund his repo or securities loan (ie, he will give the cash proceeds in exchange for the security).

When the short-seller eventually decides to close out his short position, he will have to re-enter the cash market to buy back the shorted security, in order to return it to the repo or securities lending counterparty from whom he borrowed it.

Short positions are not riskless. While the short-seller is running his short position, he is exposed to the risk that the price of the security may rise, in which case, he will have to buy the security back at a price higher than he sold it, which will mean a capital loss. A short position is riskier than a long position since the maximum capital gain on a short position is limited to the price of the security (given that its price could in theory fall to zero before he buys it back), while the maximum capital loss is infinite (given that there is in theory no limit to the rise in the price of the security).

In addition to the risks on a short position, a short-seller faces a net running cost. While the short position is open, the short-seller will accrue a daily loss at a rate equal to the coupon on the security, since the daily accrual of coupon interest on the security will add to the eventual cost of buying it back.

However, this loss of accrued interest will be offset to some degree by the accrual of a return on the cash given to the repo or securities lending counterparty, which should earn the special repo rate on the security being borrowed. The differential between the coupon rate and the repo rate is called the "cost of carry". Given that coupons are typically larger than repo rates (because coupons are for longer maturities than repos and yield curves are usually positive), the cost of carry on most securities is a net loss to short-sellers (ie, they are losing more coupon interest than they are earning on their repos or securities borrowing).

A short-seller may incur additional running costs if he is unable to locate the security in the cash market when he tries to buy it back. In this case, he will be unable to return the security to his repo or securities lending counterparty. Lack of supply is such a significant risk in the case of illiquid securities like corporate bonds that short-selling is rare. However, difficulties are also likely to be experienced in closing out short positions in more liquid securities if prices rise sharply and cause a collective rush of short-sellers into the cash market to buy back securities, in what is known as a "short squeeze".

Because the risks involved in running a short position are greater than those in running an equivalent long position, and because of the running costs, short selling is not a casual activity and short positions will always be opened cautiously.

Selling something one does not own may sound counterintuitive but short selling is a fundamental trading technique which performs an essential function in the financial markets. The reasons for taking short positions include:

Market-making - It has been explained that, if market-makers in securities quote selling prices continuously - allowing investors to buy securities on demand - they will often have to sell issues to investors which they do not hold in their inventory and which they cannot or do not wish to buy immediately from others in the market.7 The lag in buying creates a short position. Similarly, if market-makers quote buying prices continuously - allowing investors to sell securities on demand - they will often accumulate long positions which they cannot or do not wish to immediately sell back to the market. Instead, they may wish to hedge these long positions and will do so by taking short positions in issues with similar maturities. Debt management agencies universally recognise the need of market-makers to be able to take short positions and, as mentioned already, often provide special repo facilities to facilitate short-covering where the market cannot satisfy borrowing demand.

Hedging - A short position in one security is taken to provide an equal and opposite risk to a long position in another security or in a derivative such as a futures contract or an interest rate swap, so that changes in the value of the long position are substantially offset by opposite changes in the value of the short position in response to the same underlying price movement.

Arbitraging - Creating what appears to be a long position hedged by a short position but where there is a riskless profit to be extracted from the difference in the costs of the two offsetting positions.

Trading - Anticipating a fall in the price of a security by taking a short position, with the intention of buying back later at a lower price. Such short-selling can be motivated either by:

Considerations of relative value, where the price of a security is out of line with comparable securities but is expected to move back into line; views on absolute value, where all the securities from a particular issuer are seen as overvalued.

Anticipating a divergence or convergence in the prices of related instruments by taking combinations of matching long and short positions:

"Spread" trades between two securities with the same maturity, or between a security and a derivative instrument, to profit from the expected divergence or convergence in the levels of two yield curves;

"Yield curve" trades between two or more securities at different points on the same yield curve, to profit from an expected change in the slope or shape of the curve.

All these short-selling activities are key to efficient price discovery, the accurate valuation of financial assets and the prevention of asset price bubbles (markets without short-selling are much more prone to bubbles). Short-selling also generates valuable liquidity for other users of the financial markets. It is therefore a legitimate and desirable market activity, and there is an essential symmetry of function between long and short positions.

It is sometimes alleged that short-selling is intrinsically destabilising in that, more than any other trading activity, it can exacerbate financial crises by unduly amplifying price falls, fuelling price volatility and creating settlement failures, thereby contributing to disorderly markets and threatening financial stability.

The evidence however tends to point the other way. Studies in the equity market have shown that bans on short-selling have been followed by steeper price falls, increased volatility and wider bid-offer spreads. It is also the case that overshooting prices, price volatility and settlement failures can occur when prices rise rapidly on a wave of exuberant buying. In other words, the buying and selling of long positions can disrupt markets, and given the relative scale of long and short positions, the liquidation of long positions is likely to be a far more serious driver of falling prices. On the other hand, short positions may put a floor under prices which are falling as a result of long positions being liquidated. Short-sellers eventually have to re-enter the market as buyers. They will do so when prices reach target levels and will be incentivised to do so by the cost of running short positions.

Even ignoring the possibly perverse consequences of regulatory restrictions on short-selling, the likely cost, in terms of long-term damage to market efficiency and liquidity, of permanent restrictions on what is generally a legitimate and desirable market activity seem disproportionate to the infrequent problem of market disruption, even when those episodes are severe. Unusual events should be managed with special measures.

It is also questionable whether short-selling restrictions would be effective in the case of securities on which derivatives such as bond futures are available, given that these instruments provide an alternative means of taking short positions.

Concern about short-selling has prompted proposals for increased transparency, specifically a regulatory requirement that market users should publish or report their short positions. In largely institutional securities markets which are well served by publicly-quoted, exchange-traded derivatives, it is unlikely that lack of public information on short positions hinders the incorporation of negative expectations into prices. There is therefore no real market need for greater transparency about short-selling. Indeed, immediate public disclosure of short positions is likely to have an adverse impact on liquidity by causing market users to reduce the size of their positions.

There may be a case for more information to be provided confidentially to regulators about the scale of short-selling in the fixed-income market, in order to allow the monitoring of systemic risk and identification of potential market abuse. The most appropriate measure for regulatory purposes would be net short positions, ie short positions net of short covering. While net shorts positions would overstate intentional short-selling (given that some net short positions would be uncovered only because of difficulties in borrowing), the changes in this number would allow regulators to gauge the likelihood of abusive shortselling. There would seem little harm in publishing aggregated data on gross short positions after a suitable delay.

It has also been suggested that limits should be imposed by regulators on short positions. In terms of policy, such a suggestion ignores the symmetry of function between long and short positions, and betrays an inflationary bias against price falls which assumes short-selling to be inherently undesirable. In practice, the implementation of limits would be fraught with problems. It would be difficult to fix the boundary between acceptable and unacceptable short positions, and therefore set limits that do not constrain market liquidity. Such limits would also have to be global (ie, one limit per institution), given the functional fungibility of financial instruments. However, global limits are unlikely to be able to restrain the short-selling of particular securities to the extent that might be desired by regulators. SLT

The White Paper was written by Richard Comotto for the International Capital Markets Association. The full paper is available to view at www.icmagroup.org

Easy steps

In the second part of our look at marketing hedge funds, Merlin Securities examines the four stages of hedge fund development

ANALYSIS

Once hedge funds have a firm understanding of the various types of potential hedge fund investors, the next step is to tailor their marketing programme to attract the types of investors most appropriate for their stage of growth, their size and their level of institutional preparedness – that is, the robustness of their platform in terms of operations, risk management, controls and so forth.

Hedge funds should approach their marketing programme in roughly four stages, as highlighted in the diagram on page 20. These are not meant to represent unbending rules or firm boundaries, but rather to serve as a guideline to understanding how much attention a fund should be committing to attracting the right type of investors at the right times. Additionally, the stages should be used as a guide to help managers think about what aspects of their marketing programme need to be ramped up as they move to each step of the spectrum.

Stage 1, Launch and initial fundraising, represents the very early days of a fund's development, including the prelaunch activities of securing initial investment capital. The types of investors are typically individuals known personally to the manager or seeders, which require only a baseline of institutional preparedness.

Stage 2, Getting beyond retail, should also take place relatively early in a fund's lifecycle, ideally within the first 180 days. At this stage, managers have established a groove, the fund is functioning well on a day-to-day basis, core personnel and systems are in place and the fund has established clear marketing materials for targeting entry-level institutional investors.

Stage 3, The institutional threshold, represents a significant hurdle for most funds. At this stage, managers have successfully gotten several small institutional commitments, perhaps from family offices, consultants and third-party marketers. Now they are ready to break into institutional investors who will require significantly more. We have written extensively this year about the many requirements that come into play at this level.

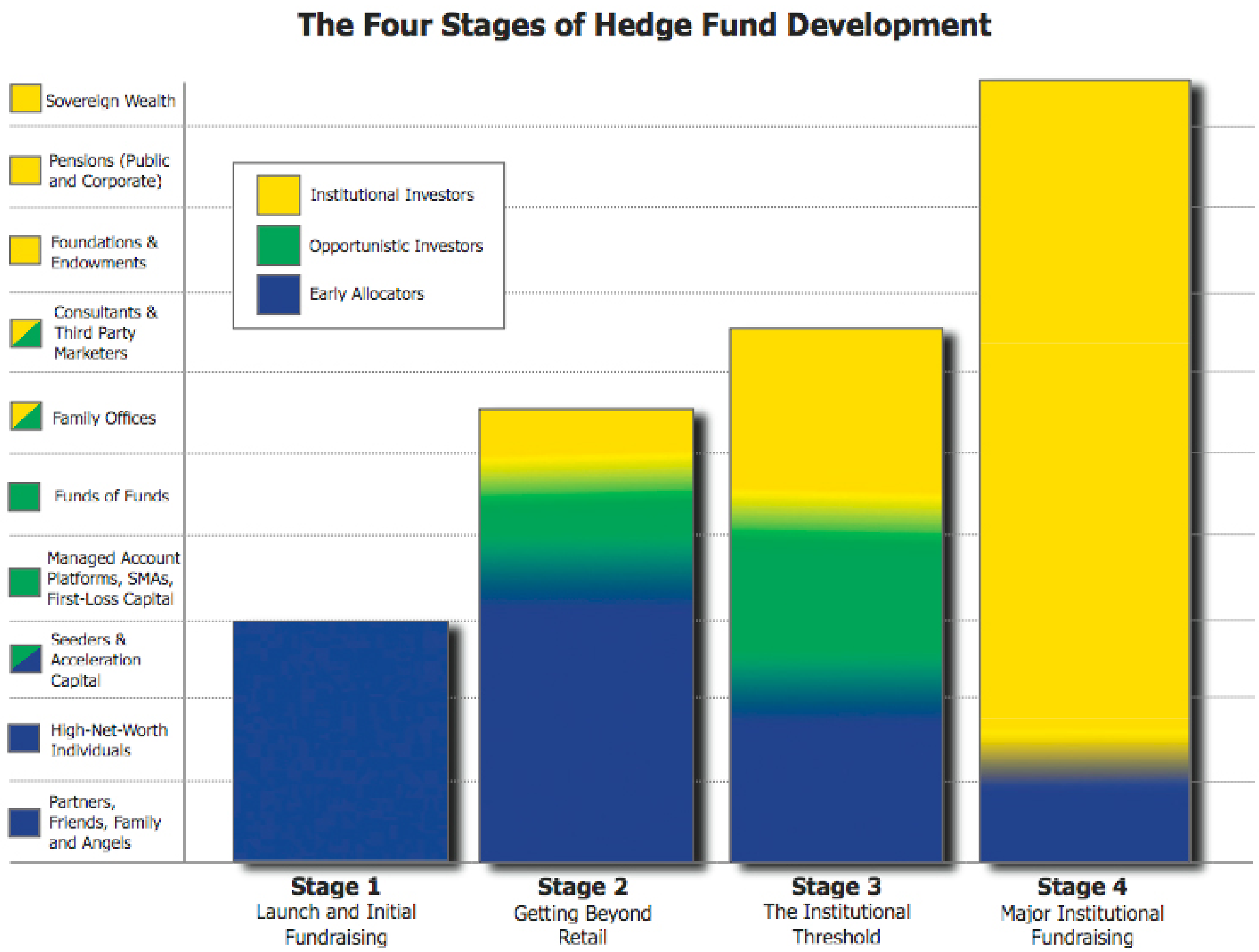
Stage 4, Major institutional fundraising, is only attainable once all of the aforementioned requirements that we have outlined this year are satisfied: the manager must be able to articulate their "edge," adhere to best practices and demonstrate a significant track record of repeatable performance with minimal volatility. Even when all these conditions are met, getting institutional capital is difficult and takes significant time. In today's environment, institutions can take many months reviewing a small number of funds and ultimately pass on most of them. When they do commit, however, these investors typically bring very significant capital to the table.

It is critical that funds understand which stage of development and growth best describes them and that they then focus their efforts on the respective targets. Just as seeders are inappropriate targets for a $10 billion fund, pensions are not the optimal target for a $1 million startup fund without a track record. Time spent marketing is valuable and should be treated as such.

In order to advance through the four stages, managers need to demonstrate increasingly that their infrastructure is robust, the investment process and results are repeatable, and that the fund is truly running a business. A fund's collective marketing efforts, outlined in the next section, should reflect these criteria.

Marketing across the stages

First, some simple definitions. Marketing, sales and communications are three terms that are



often interchanged, but they have distinct definitions:

- **Marketing** represents a firm's collective efforts to reinforce existing relationships and engage new opportunities. Marketing encompasses both sales and communications.
- **Sales** is the private introduction of the firm and its relevant product offerings.
- **Communications** is the public introduction of the firm's brand and range of products.

While sales and communications are different disciplines that produce different results, they are naturally symbiotic. When synchronised, they amplify each other and the overall marketing programme.

As funds progress through the stages of their development, a number of marketing activities need to be ramped up at each stage. Examples of the types of sales and communications efforts that funds should think about as they move through the spectrum include:

Sales activities

- Maintaining ongoing dialogue with existing clients for additional funding
- Encouraging existing clients to introduce new potential investors
- Consistent communication with strategic partners about business growth and fund performance
- Supporting foundations and charitable organisations and joining their boards (activities which, importantly, foster enormous personal growth as well)
- Maintaining connections with university endowment groups and alumni
- Developing relationships with the senior management of companies held in portfolio

Communications activities

- Upgrading pitchbook content and design to reflect the fund's size and sophistication
- Refining and improving investor letters and broadening the distribution list
- Upgrading the website
- Getting membership to additional investor databases
- Speaking and attending investor conferences
- Creating and distributing white papers that demonstrate thought leadership
- Developing and fostering relationships with key industry media
- Attending prime broker capital development events **SLT**

Conclusion

Clearly the landscape has changed dramatically for hedge fund managers and the investment community over the past several years. And so, too, have the investment approaches of each level of the spectrum changed. For hedge funds seeking to reach the next level of AUM, it is important to understand where the fund is in its lifecycle, which investors should be targeted and what each of those investors requires. Only then can a fund begin to organize its overall marketing strategy to meet the increasingly stringent investor requirements.

European Beneficial Owners' Securities Lending Summit

continued from p1

"We are all in this together," explained Duff Godon. "Beneficial owners have not been too harshly criticised, so they can use that strength to ensure the damaging rules do not come in."

The fact the industry has become more transparent was highlighted by another member of the Data Explorers team, Charlotte Wall, managing director, EMEA sales and account management.

In her presentation on the history of the securities lending market, she showed how improvements in the levels of reporting meant that much more information was available compared to just five years ago - where the data simply isn't available to compare the conditions of the market.

The general feeling about the state of the securities lending market was broadly positive. Although 2010 may not have been as busy as some people expected, it was going in the right direction.

"If there was any way to describe 2010, it would be as one of the most exciting boring years ever," said Tejash Patel, executive director at Morgan Stanley. "There were high expectations for 2010, but that's not exactly how it played out - from a hedge fund perspective, the words to use have been confusion, conviction and volatility... The changing atmosphere in investor, political and regulatory landscape has made it a tough year for shorts."

Andrew Jamieson, head of equity finance EMEA at J.P.Morgan said the slow growth was entirely down to regulatory uncertainty: "At the start [of 2010] everyone was very bullish that this was the recovery, but the regulatory change has stalled that.

"I'm still not very bullish. There is an incredibly amount of uncertainty out there. But we are making progress and we are seeing the investor community - pension funds in particular - coming back."

Liquidity remains an issue for the market, and the return of event-driven hedge funds will further stimulate growth, added Christie.

The event, held at One Great George Street, London, was considered well-attended, with around 210 delegates, of which 50 represented the beneficial owner community. **SLT**

SunGard London City Day

Date: 23 September 2010
Location: London
Website: http://events.tenfor2010.com/citydays/london.aspx

SunGard is engaging with key customers and industry players to determine how best to meet immediate challenges and help prepare you for the new business priorities which lie ahead.

4th Annual Collateral Management Conference

Date: 5-6 October
Location: Amsterdam
Website: www.jacobfleming.com

A number of high-profile defaults, volatility in the financial markets and heightened concerns over counterparty credit risk have placed great strain on many banks' collateral programmes and have highlighted the need for a new approach.

Hong Kong Securities Financing Forum

Date: 7 October 2010
Location: Hong Kong
Website: www.dataexplorers.com

Data Explorers' Securities Financing Forum in Hong Kong is taking place on Thursday, 7th October 2010. Our Global Securities Financing Forums are known throughout the industry as THE event to attend for insightful analysis that highlights specific challenges and opportunities facing the securities financing market.

27th Annual RMA Conference on Securities Lending

Date: 12-14 October 2010
Location: Boca Raton Resort & Spa in Boca Raton, Florida
Website: www.rmahq.org

The Boca Raton Resort has always been one of our premier conference locations. It was the site of the very first RMA Conference and continues to be the foremost favorite venue. We know you'll enjoy the newly renovated Boca Beach Club. It is quite a dramatic transformation!

Finadium 2010 Conference

Date: 19 October 2010
Location: New York
Website: www.finadium.com/site/conference_1010.php

This event highlights best practices and emerging trends in the prime brokerage, securities finance and asset servicing industries.

If you would like your event featured here and on our website
contact: news@securitieslendingtimes.com

Industry Appointments

Richard Allin has been named senior vice president for Asia for SunGard's Astec Analytics business unit, which specialises in providing market information solutions for the global securities financing industry. Based in Hong Kong, Allin will be responsible for running SunGard's Astec Analytics' operation in Asia.

Allin has more than 20 years of experience in the financial software and services industry. Prior to joining SunGard, he held positions with State Street, Fidelity Investments, Trema and Investors Capital.

Paul Hanley has been appointed by Citi as prime finance head of sales and capital introduction for Europe, the Middle East and Africa.

He joins the company from GLG where he was chief executive of the fund of hedge funds group. He was previously head of prime brokerage sales at Morgan Stanley.

Harvey will report to Mark Harrison, Billy Macaluso and Andres Recoder.

BTIG Ltd, a broker dealer specialising in institutional trading and related brokerage services, has expanded its Global Fixed Income team to include a London-based team focused on emerging markets complementing the current US team. The team led locally by emerging market veteran **Darren Reiss** includes **Russell Scott**, **Cornelia Colonius** and **Alpesh Lad**. They will report to Alex May, global head of emerging markets.

Reiss joins as managing director and head of the emerging markets fixed income sales team in London. Reiss' career in fixed income markets spans 18 years. He joins BTIG from Knight Libertas, where he was a director on the institutional Fixed Income sales desk. Prior to Knight Libertas, Reiss was a director of HSBC in the emerging markets sales team for eight years. He started his career at Hambros Bank trading investment grade credits. Reiss brings a number of deep relationships with dedicated emerging markets accounts.

Scott joins as managing director in the emerging markets fixed income team as head of CEEMEA trading. Scott has 16 years of emerging market credit trading experience. Prior to BTIG, Scott served as executive director in the emerging market trading team at UBS. He also held roles at HSBC trading emerging market fixed income and credit derivatives, and Lehman Brothers, where he was a director in fixed income trading. Scott started his career at ING, where he spent a total of eight years in emerging markets trading.

Lad joins the Emerging Markets Fixed Income Group in London with 15 years experience in emerging markets corporates, sovereigns and structured products. Lad's last role was as executive director, emerging markets structuring and distribution at UBS. Prior to UBS, Lad was at HSBC and Merrill Lynch. He began his career at JPMorgan Chase, where he worked for seven years in the emerging markets structuring team.

Colonius joins BTIG's Emerging Markets Fixed Income Group in London with nine years experience in emerging markets on both the buy and sell side. Colonius' last role was as director of HSBC in the emerging markets sales team covering European pension and hedge funds. Most recently she had joined the trading floor as product specialist and spot trader at HSBC Brazil in Sao Paulo. Colonius started her career at Deutsche Asset Management (now Aberdeen Asset Management) as a junior analyst, where she focused on emerging market research and portfolio analysis.

Agio Technology, a provider of managed IT services for premier hedge funds, has appointed **Nicole Nakashian**, former executive director at UBS Investment Bank, as managing director, client services.

"Nicole was our number one choice to lead Client Services since our inception," says Bart McDonough, CEO of Agio Technology. "She is very relationship oriented. She'll go through as many hoops as needed to get a client's problem solved. Clients know that and trust that. That responsiveness and caring for the client gives me great confidence she is the right person for the job of ensuring client satisfaction. That attribute, mixed with her deep knowledge of hedge fund dynamics, made her the perfect pick."

Citi has appointed **Steve Pitkin** as head of investor services for its Hedge Fund Services unit within Global Transaction Services.

Reporting into Mike Sleightholme, global head of hedge fund services, Pitkin is responsible for providing leadership for Investor Services globally within the Hedge Fund Services business. His focus will be on enhancing Citi's Investor Services proposition, growing capabilities in key markets and developing Citi's operating model and technology to improve client and investor experience and Firm profitability and controls.

Pitkin joins Citi from Citco Fund Services, where for the past five years he was global head of investor relations. In that position, he managed a team of 550 professionals in 13 locations around the world, servicing more than 550 clients with over 2,600 funds.

The Depository Trust & Clearing Corporation (DTCC) has announced that **Robert E. Garrison** will join DTCC in the position of chief development officer for its Information Technology division. He will officially start in October.

In his new position, Garrison will report to Jacob Feuchtwanger, DTCC's chief information officer. Garrison has spent 25 years at Morgan Stanley working in various technology leadership positions.

Stephen Pak has moved from Credit Suisse to become the new head of regional capital introduction at UBS' prime brokerage division.

Based in Hong Kong, Pak will head up a team that introduces Asian hedge funds to potential investors. He reports to Ashley Jarvis, global head of business and capital consultancy at UBS prime brokerage.

UBS has seen a number of changes in personnel in recent months, with a number of staff being poached by rival organisations and a raft of new hires.

"The whole nature of the industry and what clients want have been changing in the last couple of years," said David Gray, the bank's head of prime services in Asia-Pacific. "We have to move away from the generalist type of sales approach and instead moved toward seeking out and employing specialists."

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60 Second Resumé

Surendra Patel

Meet Surendra Patel, a motivated professional with over a decade's experience in the field

Tell me a little about yourself

With an investment banking career spanning nearly 10 years, I have had exposure to various products and areas, for example: FX options, prime brokerage and my last roles where within the collateral management field, specialising in securities lending.

I am an enthusiastic self-starter, a motivated and team orientated experienced professional with a 'can-do' attitude and a proven ability to learn quickly, work under pressure and to a high standard. I thrive on new challenges and look to seize opportunities when they arise.

What was your last position in the industry and what did you enjoy most about it?

My last role was a collateral management position within the equity finance area at Lehman Brothers. It was a high volume and high pressure role, which allowed me to gain a valuable insight into a lot of the products surrounding the securities lending business - for example, both cash and non-cash collateral, repos and triparty. The continual learning and exposure to these new products gave me great enjoyment. Also, the client interaction, both internal and external gave me great pleasure as did the fast paced, deadline driven environment I was part of, which was also very satisfying.

What area are you looking to get back into?

I would relish the chance to get back into the equity finance area of collateral management, but also the opportunity to enhance my collateral management product knowledge by getting into OTC derivatives collateral management or the prime services collateral management space, would be ideal.

What do you feel you could bring to a future role?

I feel with my vast experience and the skills I have gained over my investment banking career and the ones I have gained during my time away from banking would be an excellent addition to a role. My hard working mentality, my ability to learn quickly, coupled with my determination to succeed would allow me to make a positive impact to a role my adding value.

What do you feel the industry needs most?

The industry needs to ensure that as certain areas within securities lending are returning to pre-crisis levels, the "green shoots of recovery" should be nurtured and not "genetically modified" to grow too quick. This I feel can be done within the strict guidelines and controls that many banks operate within. Hopefully these institutions have seen what can happen when things go bad and have seen the consequences.

Contact Surendra

http://uk.linkedin.com/pub/surendra-patel/23/167/3a5

To be profiled please email justinlawson@securitieslendingtimes.com

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