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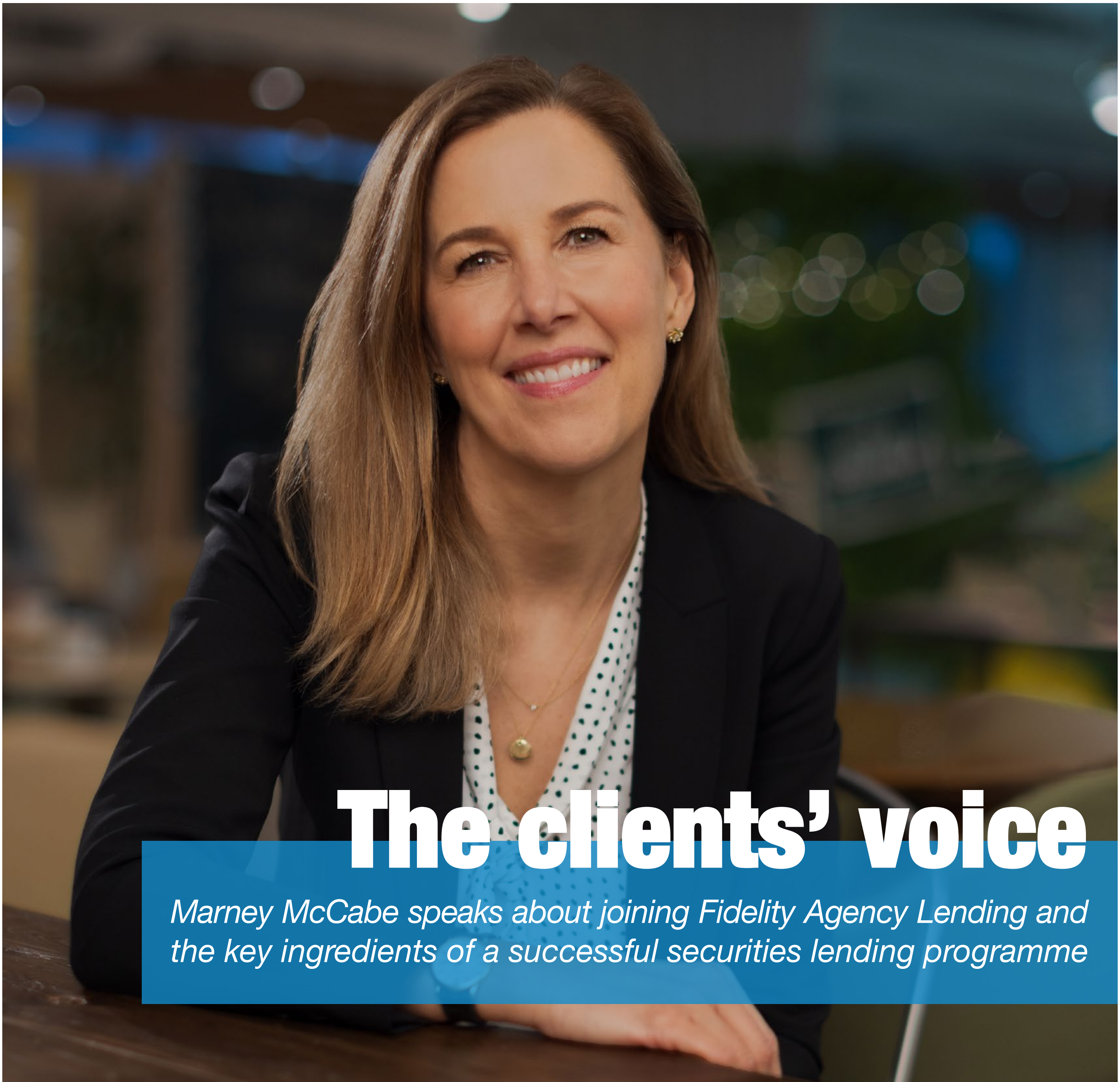

The clients' voice

Marney McCabe speaks about joining Fidelity Agency Lending and the key ingredients of a successful securities lending programme

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Women in Securities Finance rings closing bell at NYSE

Women in Securities Finance (WISF) culminated its five-year anniversary celebration by ringing the closing bell at the New York Stock Exchange (NYSE).

Celebrating the milestone, 100 guests — including active members of the group and supportive allies — gathered on the NYSE floor to watch as WISF leaders rang the closing bell to signal the end of the trading day.

The NYSE podium was graced with the WISF leadership team, including the group's co-founders Elaine Kim Benfield, Arianne Collette and Jill Rathgeber.

Also in attendance were chapter leads representing Boston (Christel Carroll, Betsy Coyne, Brooke Gillman and Marney McCabe), Chicago (Lori Paris and Colleen Kenney), Toronto (Roanna Kim and Mary Jane Schuessler) and London (Ina Budh-Raja).

This marks the final event in a series of celebrations regarding this milestone for the group.

Previously, the network came together in a Market Open Ceremony hosted by the London Stock Exchange Group. Following this, the group rang the Toronto Stock Exchange opening bell.

Rathgeber, director of securities finance product development at BNY Mellon, says: "It was an honour to be able to ring the NYSE closing bell and a perfect way to commemorate the fifth anniversary of Women in Securities Finance.

"It has been an amazing experience to watch WISF develop and grow, and I am grateful to be on this journey with my co-founders and our inspiring and dedicated leadership team. I look forward to seeing what the next five years brings."

The mission of WISF is to create a community to foster connections and promote the advancement of women in the securities finance industry. The group was formed in early 2018 and is open to all members of the securities finance community.

Global PSSL for UN Pathways to launch 3P Transparency

New principles on transparent public, private and polycentric collaboration in securities finance will be launched as part of a project by Global PSSL for UN Pathways.

The 3P Transparency project is expected to provide a long-term foundation for collaborations and include guidelines for letters of intent, memoranda of understanding and apportionment of financial costs.

It also aligns with the United Nations Secretary General's call to weed out greenwashing and dishonest behaviour in sustainable finance.

These principles will operate across a transparent and sustainable trillions finance agenda, which aims to enable stakeholders to consciously identify common goals, conflicts of interests and ways of working together through collaborations and partnerships.

The 3P Transparency project is set for release in the first half of 2023, after a research-driven recommendation that was subject to peer review within the Global Principles for Sustainable Securities Lending for United Nations Pathways (Global PSSL UN Pathways) programme.

BNY Mellon launches Korea pledge model

BNY Mellon has gone live with its enhanced Korea pledge product on the firm's International Collateral Management platform.

With the enhanced Korea pledge model in triparty, the firm says that equities and Korean treasury bonds (KTB) can be utilised more efficiently as collateral.

This can be done under BNY Mellon's standard pledge arrangements with real-time security interest pledge marking.

BNY Mellon indicates that with a recent amendment introducing tax exemption on KTBs in South Korea, the asset becomes more appealing to support a firm's collateral obligations.

CEO of clearance and collateral management at BNY Mellon Brian Ruane says: "We are

delighted to announce that the enhanced Korea pledge product is now live on our International Collateral Management platform."

BoE Money Markets Committee reflects on settlement inadequacies for sec finance trades

The Bank of England Money Markets Committee has highlighted high rates of settlement failure prevailing for securities finance trades.

Results from an informal market survey conducted across ISLA members for securities lending transactions between 2019 and October 2022 found that for closing leg trades, settlement rates were generally around 85 per cent for both equities and fixed income loans.

The Committee reported that the settlement discipline regime component of the Central Securities Depositories Regulation, implemented in February 2022, has had some positive impact on these settlement fail rates, pushing settlement rates up to 90 per cent for return leg trades for equities loans.

For open leg trades, settlement rates were typically higher, falling in the 95 to 97 per cent range for equities and fixed income transactions.

For equities loans, the survey finds that the primary reason for settlement fails in the return leg was typically lack of access to stock. For fixed income lending, the primary driver was lack of liquidity in the corporate bonds market.

These concerns about settlement efficiency also extended over into the repo marketplace. Notwithstanding a rise in settlement efficiency between May and September 2022, there was a tangible rise in fail rates over the last fortnight of September and into October linked to the rise in gilt repo volumes around the time of the UK mini-budget and the resultant surge in market volatility.

These findings were discussed at the MMC's most recent meeting, held on 12 October. The minutes of this meeting were published recently.

Since the last MMC meeting, Euroclear has taken some steps to address these concerns, including an extension of the DvP settlement window and the release of its autosplitting facility to support partial settlement in November 2022.

Concerns around excessive settlement fail rates in securities finance markets were discussed in more detail in a panel at the International Securities Lending Association (ISLA) post-trade conference in London on 1 November 2022, alongside inefficiencies currently prevailing in know-your-customer validation processes and client onboarding.

EU Council revises mandatory buy-in rules

The Council of the European Union plans to make EU securities settlement more efficient after member states agree on a proposed update for CSDR.

It looks to achieve this goal through simplifying requirements and clarifying authorisation processes related to the Central Securities Depositories Regulation (CSDR).

The Council highlights the "burdensome" requirements of passporting that hinder cross-border settlement, leading to minimised competition and reduced choice.

It says a newly proposed regulation would clarify that it is the home member state — where the CSD is authorised — that will decide on the CSD's application to provide cross-border services.

Where the CSD's activities, in at least two other member states, are considered to be of substantial importance for the functioning of the securities markets and the protection of investors, the regulation specifies that a college of supervisors will be set up.

This will facilitate the exchange of information between supervisors and ease cooperation between member state authorities.

The Council also aims to shorten the timeframe for the passporting process and to clarify its provisions, facilitating the delivery of a broader scope of services across the member states.

Significantly, the proposal looks to streamline rules on mandatory buy-ins, highlighting that the regime would be "a new measure of last resort", to be activated only in the case where the "level of settlement fails would be substantial in the EU".

In these circumstances, the mandatory buy-in regime will come into effect where a transaction has failed to settle at the end of a prescribed period and the buyer of the securities could be forced to repurchase them elsewhere.

The failing party would then be required to meet any price differential between the original and new transaction and all costs of the mandatory buy-in.

The proposal includes additional provisions relating to CSDs' ability to access banking-type ancillary services from other authorised CSDs to facilitate settlement in non-domestic currencies.

In addition, the proposal presents rules to ensure that authorities in the EU have adequate powers and information to monitor risks in relation to EU and third-country CSDs, including steps to enhance supervisory cooperation.

Today's agreement — reached by EU member states' ambassadors — will allow the Council to start negotiations with the European Parliament to agree on a common text. The European Parliament is still in the process of adopting its position.

Transactions settled by EU central security depositories in 2019 reached approximately €1,120 trillion, according to the European Commission.

Clarity provided on EMIR Refit

The European Securities and Markets Authority (ESMA) has clarified legal provisions on reporting and data management under the amended EMIR Refit rules.

Guidelines provided by the financial markets regulator aim to further enhance the harmonisation and standardisation of reporting under the upcoming European Market Infrastructure Regulation (EMIR) — which is set to go-live on 29 April 2024.

The enhancement of harmonisation and standardisation is expected to contribute to the high quality of data necessary for the effective monitoring of systemic risk, in addition to containing costs along the reporting chain.

The final report contains feedback received from stakeholders on key elements of ESMA's consultation paper on EMIR Refit guidelines published in July 2021.

In its recent paper, ESMA clarifies aspects of the regulation concerning the transition to reporting according to the revised regulatory and implementing technical standards (RTS and ITS) on reporting.

ESMA explains how counterparties should update all of their outstanding derivatives at a trade and at a position level in the course of the transition period, and the relevant action types that should be used.

The regulatory adds that the transition period "does not impact in any way the obligation under Article 9 of EMIR to report the relevant events by T+1", and that "all the reports submitted after the start of reporting under the revised technical standards will have to comply with the amended requirements".

The final report also pinpoints one respondent who questioned what actions a trade repository (TR) should take for trades that are not updated at the end of the transition period.

In this respect, ESMA says it will be monitoring the situation during the transition period and may suggest any actions deemed necessary. However, the expectation is that all counterparties comply with the 180-day deadline.

The final report on guidelines provides further explanation on issues regarding the number of reportable derivatives, intragroup derivatives exemption from reporting, and ensuring data quality by the counterparties and the TRs, to name a few.

OCC Stock Loan Programs

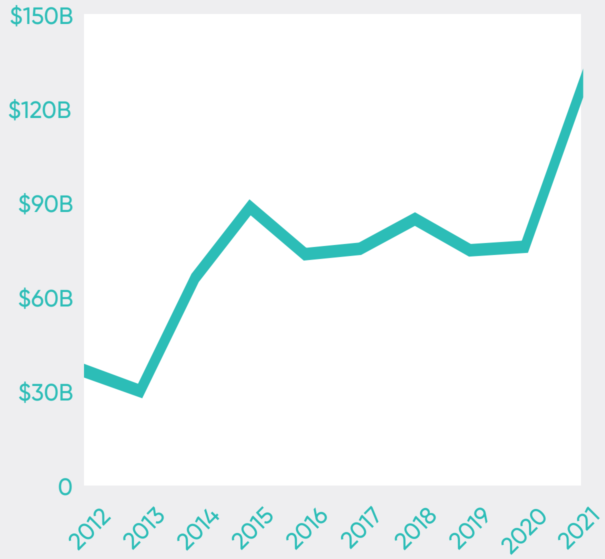
Key Benefits

- Counterparty disintermediation
- Expanded credit and trading allowances for cleared activity
- Risk weighted asset savings of approx. 95% compared to uncleared stock loans
- Margin offset
- Automation and streamlined operations

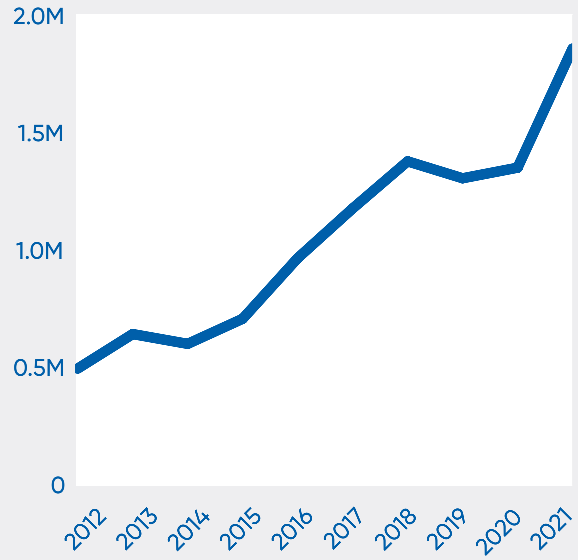
79
HEDGE LOAN PROGRAM MEMBERS

125B
AVERAGE DAILY LOAN VALUE AT YEAR END 2021

Annual Notional Value of Loans



Annual New Loan Transactions



For more information about OCC Stock Loan Programs, visit theocc.com

ESMA will continue to engage with the market participants with a view to clarifying any remaining doubts and to facilitate a smooth transition to reporting under EMIR Refit.

LSEG to acquire Acadia

The London Stock Exchange Group (LSEG) is to acquire automated uncleared margin processing provider Acadia, subject to regulatory approval.

The acquisition furthers LSEG's strategy to enhance and grow its multi-asset post-trade offering for the uncleared derivatives space.

LSEG has held a minority stake in Acadia since 2018 and has supported the business in driving growth in recent years.

Acadia provides risk management, margining and collateral services to global financial institutions for the uncleared derivatives markets.

The firm's risk and margining products span all over-the-counter (OTC) derivative asset classes and provide connectivity to market participants.

The transaction is expected to strengthen LSEG's provision of resilient and systemically important financial market infrastructure to its customers, says LSEG.

Both firms say they share a commitment to an open model, giving customers a choice as to how they process trades.

Following the completion, Acadia will be part of LSEG's post trade division, with Acadia CEO Chris Walsh reporting to Daniel Maguire, group head of post trade at LSEG.

Commenting on the news, Maguire says: "The acquisition of Acadia is part of LSEG's strategy to enhance and grow our multi-asset post-trade offering for the uncleared derivatives space.

"Our customers are looking for more ways to optimise their financial resources and Acadia's services enable significant efficiencies in risk management, margining and collateral. I look forward to working with Chris and the team at Acadia to continue to innovate and drive efficiencies across the derivatives landscape."

ECB extends liquidity lines with non-euro central banks

The European Central Bank (ECB) has extended its temporary repo lines with several non-euro central banks, as well as its temporary swap line with Poland.

Due to expire on 15 January 2023, the repo and swap lines have been extended to 15 January 2024. The size and operational parameters of the individual agreements will remain unchanged.

The decision by ECB's governing council will see Albania, Andorra, Hungary, North Macedonia, Romania and San Marino continue to benefit from the bank's repo line.

This line allows non-euro area central banks to borrow euro up to a specified limit in exchange for euro-denominated collateral.

Under a swap line, a non-euro area central bank can borrow euro up to the limit in exchange for its own currency, which is provided as collateral.

These bilateral swap and repo lines have been established since 2020 to provide euro liquidity to financial institutions via non-euro area central banks in view of the COVID-19 pandemic and heightened geopolitical tensions triggered by Russia's invasion of Ukraine.

In respect of the persistent uncertainty stemming from Russia's ongoing war in Ukraine and the associated economic and financial repercussions on the global economy and financial markets, the lines are designed to prevent spillover effects in euro-area financial markets and economies and safeguard the transmission of the ECB's monetary policy.

Rest Super joins GPFA

The Global Peer Financing Association (GPFA) has welcomed Australian superannuation Rest Super as its newest member.

The working group aims to encourage the development of a more effective and transparent marketplace for securities financing activities, liquidity management and collateral management.

Rest Super joins the beneficial owner association with more than 30 other active buy-side organisations involved in the securities financing markets.

The firm is one of Australia's largest profit-to-member superannuation funds, it uses its size and expertise to deliver long-term investment performance to 1.9 million Australians.

Commenting on the announcement on LinkedIn, GPFA says: "We look forward to involving Rest Super in the global GPFA community, as well as in our growing Australia and Asia-Pacific member group, where networking, education and discussion of best practices among our members benefits the whole beneficial owner ecosystem."

Marney McCabe
Head of relationship management for agency lending
Fidelity Investments

The clients' voice

Marney McCabe, head of relationship management for agency lending, speaks to Carmella Haswell about joining Fidelity Agency Lending and about the key ingredients of a successful securities lending programme

Marney, congratulations on your role at Fidelity. How do you plan to shape the firm? What lessons will you bring to Fidelity and its clients that you have learnt from your time in the industry?

Thank you. I am thrilled to be joining such an incredible team and reputable firm, and equally excited about the opportunity that lies ahead for Fidelity Agency Lending. Having spent more than 20 years in the financial services industry, and the last 16 years in various market-facing roles in agency lending, I have gained a strong understanding of what institutional clients need to manage a successful securities lending programme.

Clients are looking for a provider that understands their specific requirements and ultimate goals. They need an agent that can meet their needs for data, oversight and execution, and utilise technology for efficiency and ease of business. In my position, I will incorporate the depth of the Fidelity offering and tech-driven platform to deliver a consistent experience throughout the life of the relationship — starting at the initial point of onboarding. Relationship management works closely with each client to establish a programme that is transparent and continues to operate the way it was intended, while remaining aligned with their business goals.

Lender behaviour is evolving at a rapid pace, and I plan to be the clients' voice at Fidelity as we continue to develop a comprehensive roadmap and investment in our programme offering.

How is relationship management changing in the securities lending space? What is Fidelity doing to support client requirements?

Securities lending has become increasingly relevant as the competitive landscape intensifies. Regulatory changes, low organic asset growth, continued fee compression, and increased pressure to optimise operating models are persistent challenges for many asset managers and institutional clients. We are experiencing an increase in inquiries and expect request-for-proposal (RFP) activity to grow as asset managers explore different ways to gain alpha and optimise shareholder value. Clients are feeling the downstream result of regulation, which is impacting their programme performance. Fidelity is in the position of not having to manage our book around capital restraints.

Typically, we see managers applying less than one FTE to the oversight of a securities lending programme, which makes it increasingly important that the agent can be an extension of their efforts. This is where relationship management and a comprehensive "know your client" strategy has become increasingly important. Fidelity's platform allows the relationship manager to have direct access to real-time data, resulting in intraday oversight and better solutioning.

Additionally, as lendable supply increases at a quicker rate than demand, clients are putting more emphasis on loan execution, overall performance and operational stability. At Fidelity, we are using data and advanced technology to increase connectivity and relevance with our trading counterparties, which is resulting in better performance, transparency and efficiencies for our clients.

What are beneficial owners looking for in an agent lending provider to help them deliver and meet their securities lending goals?

Beneficial owners are looking for an agent lending provider that can keep pace with the evolving industry. At Fidelity, constant and consistent investment in our programme remains a primary focus and, to date, we have addressed many industry challenges through scalable and innovative development. One example of this is a benchmarking tool that was recently added to PB Optimize that not only looks at performance, but can measure the capabilities of multiple agents, giving the lender the power of more informed decision-making and control over their lendable assets.

PB Optimize is our comprehensive fintech solution for portfolio management that can help maximise revenue with market insights, and real-time aggregated data and analytics. It has become clear that better, more advanced technology can help address change in a swift and scalable way, while also mitigating the potential risks to lenders and not compromising the overall performance of a securities lending programme.

How important is performance benchmarking in securities lending and how is this evolving as a discipline?

Performance benchmarking is one attribute of measurement of a securities lending programme and is important to make sure that an agent lending provider is meeting its revenue expectations. Historically, we have seen beneficial owners rely on their providers to perform benchmarking. However, in more recent years, we are seeing lenders looking for an independent source to provide this analysis (at an additional expense). Fidelity is responding to the need for lenders to have greater insight into the performance of a

securities lending programme and the market dynamics that are driving returns. With the use of proprietary technology, Fidelity is building solutions that can give lenders the information they need without adding extra costs and resources to their oversight model.

Clients have a fiduciary responsibility to their shareholders to ensure that the securities lending programme is aligned to the goals of the firm, and meeting performance expectations and regulatory guidelines. In addition to performance benchmarking, we encourage our clients to benchmark their providers based on service, product knowledge, investment roadmap and overall management of their programmes. Annual due diligence reviews of the business, understanding how investments are driving programme attributes, and daily transparency into the controls that drive a programme are all key to the overall performance of a client's programme.

From Fidelity Prime Services to Fidelity Agency Lending, where are you focusing your resources to deliver enhanced services to your clients for 2023?

Today, we provide a wide array of products and services to serve and support institutional clients. With our prime brokerage services, institutional clients can access unique inventory via Fidelity's businesses and institutional relationships, leverage our advanced platform technology and have access to PB Optimize. Our custody and clearing clients have access to our fully-paid securities lending programme for the opportunity to earn incremental income on portfolios. We also have Fidelity Agency Lending — a customisable, technology-driven securities lending programme that helps asset managers, hedge fund managers and other institutional clients to optimise performance for a competitive edge.

In 2023 and beyond, a commitment to innovation and to meeting the needs of institutional clients are at the forefront of our goals. We will continue to enhance the multi-agent benchmarking tool, build out compliance oversight tools, and create exception reporting and alerts. We will also leverage PB Optimize to empower our clients with market data, programme transparency and market-leading performance.

We are in growth mode. Therefore, we will continue to focus on efficient and seamless onboarding. In fact, we just onboarded our first non-affiliate client and will onboard two others in the first half of 2023.

How is technology disrupting the securities finance industry and how is this changing the way that Fidelity is engaging with the market?

Newer technologies, increased automation and richer data are leading to disruption, opportunity and transparency in the securities finance industry. The ability to lend or access supply via automated processes continues to increase. Personnel who work in middle- and back-office positions require increased real-time information to scale under increased volumes. Regulatory changes, such as Securities Financing Transactions Regulation (SFTR), Central Securities Depositories Regulation (CSDR), T+1, and, potentially, 10c-1 may create more of a need for automated, real-time processes to help comply with and meet certain requirements.

Technological innovations can have the most impact and drive change in all aspects of securities finance. In the future, distributed ledger technology may provide additional benefits that we may not fully comprehend yet. These changes may lead to T+0 settlement, 24/7 trading, reduced transaction costs, and a change in the landscape for market participants. It is certainly something we are keeping an eye on. The increased market adoption of newer technologies has reaffirmed Fidelity's belief that investing in modern technology and newer, more efficient ways of conducting securities lending business will create opportunities for our clients and our securities lending programme.

What can the industry expect from 2023 in terms of opportunities and the changing financial landscape?

There are a few themes that we experienced in 2022 that will carry into 2023. Regulation, in particular the robust US Securities Exchange Commission's agenda, will continue to be a focal point in the year to come. Fidelity will continue to work with industry groups — such as the Risk Management Association and the International Securities Lending Association — to represent what is in the best interest of the programme and our securities lending clients. Additionally, capital constraints associated with securities lending activity will continue to be a distraction and influence the performance of many lending agents. Fortunately for Fidelity, we do not share these same constraints and will continue to maintain a client-first mentality.

In terms of demand, we expect the market to adjust to the rising interest rate environment of 2022, which will result in increased market engagement, including long and short strategies that promote securities lending demand. We also expect a flurry of corporate action-driven activity and an increase in new issuances after a somewhat muted second half of 2022.

Kyle Kolasingh
Director of securities finance
RBC Investor & Treasury Services

Progress in the face of uncertainty

Despite a particularly volatile environment, securities lending continued to thrive in 2022. Kyle Kolasingh, director of securities finance at RBC Investor & Treasury Services, shares his perspective on the past year and what lies ahead for 2023

It has been a strong year for securities lending, with annual industry revenues up by approximately 15 per cent globally, based on information provided by S&P Global. While volatility inherently brings challenges, it ultimately proved beneficial for securities lending, creating openings for a diverse range of financing transactions and lending opportunities.

For the third year in a row, we saw a turbulent first quarter, which was marred by the Russia-Ukraine conflict. An important point to take from this period of 2022 is the resilience demonstrated by securities lending. The industry moved quickly to align with a range of regulatory requirements and sanctions that affected both assets on loan and those used as collateral. This speaks to the strength of the lending market and bodes well for the future, demonstrating the sector’s ability to adapt and thrive in challenging times.

As central banks started to taper their quantitative easing programmes, market participants returned to the financing market to source liquidity. This made for a healthy fixed income market, giving rise to an increased appetite for Canadian government and provincial bonds on both an open and term basis. Where flexibility in collateral was permitted and duration could be taken, beneficial owners holding such assets continued to capture significant premiums on overnight fees. Corporate bonds have also been high performers as pressure on the credit environment had a positive impact on borrower demand in 2022. We expect this demand for fixed income assets to continue in the new year.

On the equities side, exchange-traded products (ETPs) remained a popular borrow, providing a convenient way to hedge or gain sector exposure. This is a trend that we expect to continue into 2023 — particularly for high-yield bond ETPs, given ongoing market volatility and economic uncertainty. Entering the new year, continued geopolitical uncertainty across the European region, coupled with an evolving inflationary and recessionary environment throughout much of the developed world, will likely contribute to further market volatility. However, as the past has shown, such volatility brings opportunity for securities lending as financing demand adapts.

Unlocking new supply

We are seeing increased demand for enhanced reporting and data access to support more informed decision making on the part of new and existing beneficial owners. An example is corporate bonds, where current market conditions may give rise to liquidity concerns. In a rising rate environment with volatility and credit pressure, access to the right data provides beneficial owners with clearer insight into the risk and reward trade-off associated with securities lending. Close communication with agent lenders is also vitally important. We continue to foster strong relationships with our beneficial owners to ensure that their understanding of the financing market aligns with their goals and risk parameters.

Another growing area relates to the retail side of the market. The meme stock craze of early 2021 demonstrated the scale and importance of retail investors’ contribution to the financing market. This segment generated significant lending returns in 2021 and 2022. Known as “fully-paid lending” in the US, the retail segment has come to market in Canada. In particular, Canadian wealth managers are increasingly seeking opportunities to add incremental value and boost returns for their retail investor base through securities lending — a trend that is likely to continue in 2023.

T+1 and transparency

Although T+1 will not be implemented in Canada and the US until at least 2024, much of the heavy lifting to prepare for a shortened settlement timeframe will take place in 2023 through to 2024. While changes to securities lending activities are still under discussion, T+1 will ultimately reduce the time to recall a security by one day. Not unlike the move to T+2, the securities lending industry supports efforts to improve market efficiency. Other market changes planned for 2024 —

including Canadian Depository for Securities (CDS) modernisation and a potential “fails regime” on Bank of Canada government securities — point to a busy time ahead here in Canada.

The industry will be watching closely as the US Securities and Exchange Commission (SEC) wraps up its Rule 10c-1 draft legislation, which aims to provide further transparency in the securities lending market. It remains too early to say how these proposed changes will affect Canadian beneficial owners, or the Canadian market of lendable securities. However, it is likely that the capabilities built and designed by industry participants for the Securities Financing Transactions Regulation (SFTR) in the EU and UK will be leveraged and, perhaps, even enhanced.

> *"It is important to note that the creation of collateral exclusions based on ESG considerations has the potential to reduce the benefits of diversification"*

Another area that we expect to receive greater attention in 2023 is digital assets and digitised technology. T+1 may well be the beginning of a discussion leading to T+0, or same-day settlement, which could benefit from some form of distributed ledger technology. The International Securities Lending Association (ISLA) recently published a report that highlights considerations for digital assets, and this area will undoubtedly be a fascinating evolution for securities finance.

ESG isn’t going away

ESG is a topic that I discuss with clients on a daily basis. We have always recognised that securities lending promotes sustainability of the wider capital market system by providing access to liquidity and balanced views for price discovery. However, as beneficial owners have been increasingly utilising proxy voting to fulfil ESG policies in recent years, there has been much discussion of its compatibility with securities lending.

Now this discussion is evolving. Increasingly, asset managers are employing securities lending as part of their overall ESG framework. For example, they may opt for a stronger position than divestiture from a sector — taking directional positions rather than long investments. They may also regard participation in securities lending as a contributing factor to overall sustainability of the capital markets ecosystem. This has effectively taken the discussion beyond compatibility concerns to the deployment of holistic, ESG-driven investment strategies that incorporate securities lending.

There is further discussion around the potential application of ESG principles beyond investment portfolios to collateral management. It is important to note that the creation of collateral exclusions based on ESG considerations has the potential to reduce the benefits of diversification and lead to increased concentration risk, which could ultimately diminish the risk-mitigating function of a collateral portfolio.

In November 2021, the Global Alliance of Securities Lending Associations (GASLA) published a best-practices guide on proxy voting and has been working towards a refreshed version of the Global Framework for ESG and Securities Lending (GFESL), which will encompass collateral management and related topics.

When all is said and done, ESG will continue to evolve away from the familiar proxy voting dialogue to a more holistic and positive force, which will inevitably be ingrained in almost everything that we do.

Diversity makes us stronger

Looking forward, I am hoping to spend more time amplifying the diversity, equity and inclusion discussion within the securities lending industry — this is particularly important to me on a personal level based on my own background.

This year, we saw Women in Securities Finance — which recently celebrated its fifth anniversary — not only continue to champion gender diversity, but also broaden the conversation to include more universal equity and inclusion. Ultimately, greater diversity will strengthen the securities lending industry through wide-ranging perspectives and place us in a better position to face a constantly-changing market in the years ahead.

Industry associations urge review of SEC treasury clearing proposals

Bob Currie examines how the industry has reacted to SEC proposals, announced for consultation in September 2022, that could mandate central clearing for a wide array of US treasury-based transactions, potentially including repo, securities lending and UST cash securities trades

In September, the US Securities and Exchange Commission (SEC) put forward a proposed set of rules designed to enhance risk management practices for central counterparties in the US treasury (UST) market and to encourage central clearing of a wider range of UST-based transactions.

The SEC notes that the US$24 trillion US treasury market — "deepest, most liquid in the world" — is the foundation upon which so much of the US capital market is built. “Treasury markets are integral to how the Federal Reserve administers monetary policy. They are how we, as a government and as taxpayers, raise money,” says the SEC.

SEC chair Gary Gensler indicates that he is pleased to support these rules because, if adopted, “they would help to make a vital part of our capital markets more efficient, competitive, and resilient”. But these benefits are assumed in the SEC’s proposal, rather than demonstrated through clear argument based on empirical data. This is not to understate the benefits of central clearing, which have been widely articulated in Securities Finance Times. But if the SEC is to mandate central clearing for a wide range of UST-based transactions, it is important to be clear where existing risk and inefficiency resides — and how CCP clearing will solve this problem.

In making the case for the Proposed Rule, the SEC indicates that in 2017 only 13 per cent of US treasury cash transactions were centrally cleared. In the 1990s, by contrast, the Commission suggests that this ratio was significantly higher — prior to 2000, all users of interdealer broker (IDB) platforms were members of central clearing houses and their trades were centrally cleared. Since this time, the SEC maintains that there has been a significant increase in principal trading firms (PTFs) trading in this market and IDBs are taking on clearing house-like functions, even though they are not regulated as clearing houses. “This leaves our system potentially vulnerable to risks that may emanate in particular from those IDBs, PTFs, and hedge funds in the US treasury markets,” says Gensler.

Among other steps, the SEC plans to amend the standards applicable to clearing houses (or “covered clearing agencies”, CCAs) for US treasury securities, obliging each CCA to apply written policies which require direct participants to submit all “eligible secondary market transactions” (ESMTs) in treasury securities for clearing and settlement.

It also proposes selective amendments to CCA risk management standards designed, according to the SEC, to protect investors, reduce risk and increase operational efficiency.

Access to clearing

In responding to the SEC consultation proposal, Jennifer Han, chief counsel and head of global regulatory affairs at the Managed Funds Association (MFA), states that although the MFA supports the Commission's intentions to strengthen the US treasury market, the first priority should be to expand the availability of central clearing.

Without this, the MFA believes that the SEC's proposal is likely to be counterproductive, potentially reducing market efficiency and resilience by making it more difficult and expensive for investors to transact and, ultimately, increasing market concentration and risk.

With this in mind, this buy-side trade association advises that the SEC's proposals should focus initially on market segments where the benefits of central clearing are most obvious and existing market infrastructure is best able to support more central clearing — which, in the first instance, should be for bilateral repo and reverse repo transactions.

In contrast, the MFA does not believe that mandatory central clearing is appropriate at the current time for UST cash securities transactions, or that mandatory clearing should be applied for triparty repo transactions.

"Rather, the potential benefits of central clearing are less significant with respect to these types of transactions relative to bilateral repo transactions, while the costs are likely to be significant and outweigh those potential benefits," says Han. Specifically, the MFA advises that expanding the clearing mandate beyond bilateral repo transactions would "interact unfavourably" with existing practices in the areas of cash and collateral management and securities custody, for example by inhibiting same-day access to treasury securities for investment or margining purposes.

The International Swaps and Derivatives Association (ISDA) conducted a survey of market participants during 2022 to gauge the industry's appetite for additional clearing requirements for UST cash securities and repo transactions. The survey reveals a diversity of views on whether extension of clearing would improve the resilience and efficiency of the UST marketplace. Many, it noted, were generally supportive of clearing, but few supported broad clearing mandates, believing this could prompt some participants to reduce their activity or to withdraw from the market entirely, thereby reducing market liquidity. However, many did support reforms that they believed would improve efficiencies in the UST marketplace, including provision of relief under the supplementary leverage ratio (SLR), steps to improve access to indirect clearing, and the ability to post client collateral to the clearing agency. Respondents also highlighted potential for facilitating additional cross-margining opportunities between cleared cash and futures markets.

ISDA notes that the SLR, risk-weighted asset (RWA) and global systematically important bank (GSIB) surcharges are binding constraints on some banks and these regulatory overheads have prompted some firms, over time, to exit certain business lines. ISDA is therefore supportive of adjustments to the SLR and GSIB surcharges, for example, which would bring greater cost efficiency and balance sheet efficiency to banks' trading activities in the UST marketplace. "We recognise that the SEC does not itself have the ability to modify the SLR, but we strongly encourage the SEC to work with prudential regulators to implement modifications prior to finalising the proposal," says Ann Battle, senior counsel for market transitions at ISDA.

Securities lending

Commenting on the SEC's proposals, the Risk Management Association's (RMA's) director for securities lending and market risk, Fran Garritt, and chair of the RMA committee on securities lending, Mark Whipple, raise concerns that if the SEC Proposed Rule is adopted, US treasury repo transactions conducted by lending agents when reinvesting cash collateral — collateral received on behalf of beneficial owner lenders through securities lending trades — would need to be cleared through a CCA.

The RMA Council questions whether it was the SEC's intention to capture reinvestment of cash collateral through UST repo transactions under the Proposed Rule. As such, it asks the Commission to conduct further research on the impact of these proposals on agency securities lending before taking further action towards mandatory clearing.

More generally, the RMA indicates that it opposes the inclusion of securities lending trades in the list of eligible secondary market transactions that should be subject to mandatory clearing. "Owing to the razor thin spreads on US treasury securities lending transactions," proffers the RMA, "any additional capital or liquidity costs to lending agents, or requirements for additional margin or clearing fund contributions, could result in these transactions not making economic sense for any party."

For Q2 2022, the RMA's data indicates that slightly less than US$2 trillion of US treasuries were available in securities lending programmes as lendable assets, with just under US$660 billon on loan globally. For these on-loan securities, more than US$265 billion of US treasury securities were on loan against cash collateral.

"As treasury securities lending transactions are low-risk, low-spread transactions, requiring them to be cleared through the Fixed Income Clearing Corporation (FICC) would impose additional costs and margin, which could cause some treasury securities lending transactions to become economically unviable for beneficial owners or lending agents," says the RMA in its response to the SEC. "Fewer treasury securities lending transactions could lead to reduced liquidity in the overall treasury market."

Clearing models and incentives

The Securities Industry and Financial Markets Association (SIFMA) advises that the SEC should consider sequencing its approach to reforms in the US treasury clearing market in a different order. Specifically, the Commission should start with providing better incentives for firms to enter UST trades for central clearing without prematurely making it a requirement.

At root, this should begin with CCAs offering more efficient and straightforward clearing models that offer better protection for investors. With these improved models in place, SIFMA believes this will encourage more market participants to clear UST-based transactions voluntarily and will encourage greater liquidity.

According to managing director and assistant general counsel of SIFMA's asset management group William Thum, the SEC should only introduce a broad requirement to clear when it has already tested other mechanisms designed to incentivise central clearing and after these have demonstrated improvements to the operation of the UST marketplace.

Before central clearing is made mandatory in the UST markets, SIFMA says, the industry must also have a more robust clearing ecosystem that has been designed with input from all relevant stakeholders. Specifically, the SEC should "only impose a clearing mandate when FICC *and at least a second covered clearing agency* (emphasis added) are able to offer access to clearing solutions that will fulfil enhanced rule requirements and meet the needs of market participants."

Addressing a similar point, the RMA contends that the SEC Proposed Rule is likely, in its current form, to bring higher concentration risk through raising clearing volumes through DTCC-owned FICC as a single clearing entity. "The Proposed Rule, to include UST securities lending transactions in addition to UST repurchase transactions, would concentrate all of the counterparty risk associated with these transactions with a single CCA," says the RMA. "In determining whether to adopt the Proposed Rule, the RMA Council urges the Commission to carefully consider that any disruption or failure of this single CCA, whether financial, operational, or technological, would almost certainly harm beneficial owners, lending agents, borrowers, the capital markets, and ultimately, the global financial system as a whole."

Additionally, for SIFMA, the clearing model ultimately delivered through these SEC proposals must offer protection that more closely mirrors the risk management framework applicable for FCM-cleared OTC derivatives. "Although the market for US treasury transactions is very different from the OTC derivatives markets, prior to any clearing mandate being imposed, there must be an available clearing solution which provides market participants with a level of resilience and protection more like that currently provided for cleared OTC derivatives cleared through a futures commission merchant (FCM)," says Thum. "Among other things, this model should ensure that collateral posted by customers is appropriately segregated and not subject to the risk of a direct clearing member default."

Elaborating on this principle, Futures Industry Association president and CEO Walt Lukken explains that, among other requirements, FCMs must hold these funds and securities in customer segregated accounts established in accordance with the provisions of Commodity Futures Trading Commission (CFTC) Rule 1.20 (with regard to futures traded on US futures exchanges) and Rule 22.2 (with regard to cleared swaps). Specifically, an FCM must deposit futures customer funds with a bank, or other permitted depository, under an account name that clearly identifies them as futures customer funds. In doing so, it must obtain a letter from the depository which acknowledges that the FCM has deposited money or securities held on behalf of a customer.

"The depository acknowledges that such customer assets 'will be separately accounted for and segregated' on the depository's books from the FCM's own funds 'in accordance with the provisions of' the CEA and the CFTC's rules, and 'must otherwise be treated in accordance with the provisions of section 4d of the [CEA]' and the CFTC's rules," the FIA explains.

SIFMA indicates that it is also important that market participants have access to standardised documentation to govern their clearing relationships, along with industry legal opinions that address the enforceability of netting and collateral arrangements for cleared treasury transactions under applicable bankruptcy laws. "To our knowledge, no such standardised documentation or legal opinions currently exist for the clearing models currently accessible to indirect participants clearing through FICC," says Thum.

With these considerations in mind, there is a case for requiring separation of initial margin from default fund requirements at FICC that can be subject to loss mutualisation. This may improve capital efficiency for banks and bank-affiliated dealers, but may also widen participation from firms that are currently prevented from participating in loss mutualisation arrangements.

More broadly, industry commentators advise that the SEC may need to make rule changes to enable a debit under the SEC Rule 15c3-3a customer reserve formula, enabling broker-dealer direct participants at the clearing house to pass customer margin through to the CCP, thereby simplifying the mechanisms through which margin can be transferred to the CCP on behalf of indirect participants.

Costs and benefits

In concluding, the MFA observes that the costs of requiring central clearing of triparty repo transactions and cash market transactions are likely to outweigh any potential benefits. "Relative to bilateral repos, triparty repo transactions already provide for additional risk mitigants and protections due to the role of the triparty agent and related regulatory oversight of the market," says the MFA's Han.

More broadly, the MFA proposes that cash UST transactions do not present the same level of credit risk as repo transactions, which implies that a principal benefit of central clearing, namely risk mitigation, will be less obvious in these markets. This may particularly be the case for indirect clearing participants, where the MFA indicates that "certain more frequently used clearing models for cash transactions do not provide meaningful opportunities for clearing-related netting and risk mitigation benefits for indirect participants."

SIFMA believes that the SEC, and other financial regulators, need to engage in additional analysis of the US treasury market, considering all available market data, before imposing central clearing on broad portions of this market.

"Given the state of the existing clearing infrastructure, the immediate benefits of a central clearing mandate are not obvious, and more evidence is required to demonstrate how clearing will mitigate contagion and systemic risk and improve capacity and resiliency in this market," concludes SIFMA's Thum.

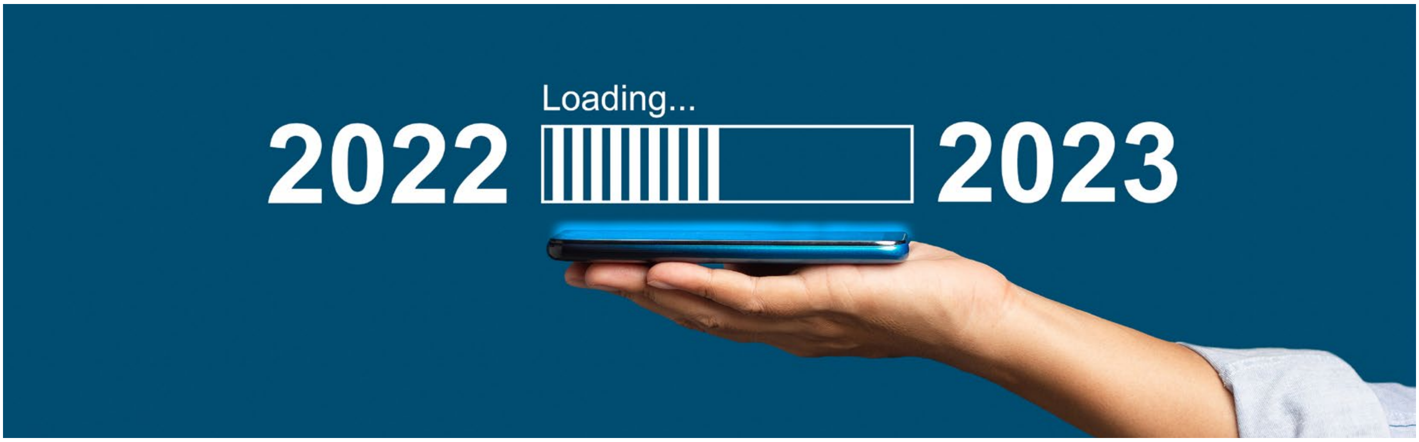
Specifically, SIFMA indicates that it has seen no convincing data demonstrating how a requirement to centrally clear, along the lines advanced in the Proposed Rule, would have fixed some of the recent liquidity problems highlighted by the SEC — for example, the "flash rally" of 2014, the stress in the US treasury repo market during September 2019 and the COVID-19 market shock of March 2020.

Like the MFA, SIFMA does not currently support a clearing requirement for UST cash transactions. In SIFMA's view, any requirement to clear cash transactions will "increase costs, generate operational complexities and reduce liquidity", without producing meaningful benefits to address perceived shortcomings in the UST cash transaction market.

Pittsburgh-based investment manager Federated Hermes questions the need for an extension of central clearing for UST-based repo trades, indicating that the SEC "does not cite any circumstances where parties have encountered difficulties in clearing and settling repurchase agreements".

Specifically, Federal Hermes believes that the SEC's Proposed Rule fails to take into account significant changes regarding clearing of triparty repo trades that have been implemented since the 2008 financial crisis. "The clearing bank handles the settlement of triparty repurchase agreements through its collateral allocation systems and [this] has resulted in a well-functioning process that already operates under severe time constraints," says Federated Hermes.

The asset manager indicates that it has also not experienced significant difficulties in clearing and settling US treasury repo trades on a bilateral basis. "These repurchase agreements are settled on a same-day, DvP basis," it notes. "[We] give instructions for the settlement of these repurchase agreements as soon as they are confirmed, so settlement generally is completed as rapidly as possible."



Reflecting on the past, preparing for the future

SFT speaks to industry representatives to gauge what the market can expect as it enters into 2023

Stepping into the new year after a storm of regulation, increasing interest rates and high volatility, the securities lending market is now bracing itself for what is to come in 2023.

Market participants map out their priorities for the year as an “aggressive” regulatory agenda is expected to bring a host of proposed rules for the buy- and sell-side. Risk-weighted assets are predicted to remain a binding constraint for many borrowers and lenders across the market, while central clearing models become a key to unlock significant liquidity.

A brisk pace

The Central Securities Depositories Regulation (CSDR) and the move to a T+1 settlement cycle in the US were key components of the regulatory landscape that impacted buy- and sell-side firms in 2022. With an objective to drive settlement efficiency, CSDR provided provisions of shorter settlement periods, mandatory buy-ins — that were postponed until 2025 after pushback from the Joint Trade Associations — and cash penalties, which came into force on 1 February 2022.

Further changes in February 2022 caused a buzz in the industry as the U.S Securities and Exchange Commission (SEC) proposed to shorten the settlement cycle to T+1, in an effort to reduce the credit, market and liquidity risks in securities transactions faced by market participants and US investors. “The move to T+1 will touch nearly every aspect of the front, middle and back offices. The accelerated timeframes will further pressure processes in security finance, and much of the industry is not ready from a technology perspective,” indicates Madhu Subbu, Clear Street’s head of securities finance engineering.

The pace of new regulation continues to be very brisk in the US and Europe, causing market participants to anticipate what regulatory challenges they will have to face in 2023. The regulatory landscape for the year will differ by region, according to Robert Lees, EMEA head of securities lending and global head of securities lending trading at Brown Brothers Harriman (BBH).

Lees reveals that, in Europe, 2023 focus areas include the implementation of the next phase of the Securities Financing Transactions Regulation (SFTR), including 31 additional data points subject to reconciliation that is scheduled to be implemented in January. Proposals to move towards a T+1 settlement cycle will be monitored closely by the industry, as evidenced by the UK government’s creation of an Accelerated Settlement Taskforce in December 2022 to explore the potential for faster settlement of financial trades.

In the US, Lee comments that the SEC’s “aggressive agenda” has resulted in many proposed rules. Although primary regulatory developments are yet to be finalised, the sector can expect to face potential mandatory reporting regime for securities lending transactions, mandatory clearance of US Treasury securities and a transition to T+1 settlement, which is scheduled to take effect early in 2024.

State Street's global head of agency lending Francesco Squillacioti expects that a significant regulatory change will come in the form of the Basel IV rules. Proposals for these rules are to be issued in 2023, with final rules likely to be implemented in 2025. A new standardised formula for securities finance transactions will have a large impact on the sector, says Squillacioti.

The new formula will take into account the benefits of correlation and diversification within netting sets of loans and collateral. This benefit will greatly reduce the risk-weighted assets (RWA) for entities that are bound by the standardised approach — generally US banks and broker-dealers, which have a 100 per cent floor.

Squillacioti also anticipates the SEC's finalised proposal for Rule 10c-1, which is expected to be released in the first quarter of 2023 after a proposal and call for evidence was issued initially in December 2021. State Street worked closely with the Risk Management Association (RMA) and the Investment Company Institute (ICI) to respond to the suggested framework for this piece of legislation.

State Street's response to the SEC's proposal indicates that the proposed T+15 minutes reporting requirement is "impractical" as the market recommends end-of-day reporting. Additionally, the firm suggests eliminating the requirement to report "lendable" shares, as State Street believes it may be "inaccurate and misleading".

Subbu believes Basel IV will provide improved approaches to credit risk, operational risk and pricing of derivative instruments. "Preparation for these challenges will be the key, as market participants move toward cloud-based workflow providers to decrease collateral management costs, ensure settlement reliability and increase securities finance profits," he concludes.

A global interest

A new year does not equate to a new agenda, it would appear. There remains a growing global interest by clients to promote sustainable environmental, social and governance (ESG) principles through securities lending programmes. For Lees, providing customers with the appropriate information to make informed decisions around ESG and securities lending remains a top priority.

In the summer of 2022, State Street's Travis Whitmore, senior quantitative researcher and head of securities finance research, revealed that institutional owners were restricting lending of companies perceived as unsustainable. The International Capital Market Association (ICMA) has also indicated that repo is playing a more active role in sustainable finance, as firms continue to develop new sustainability-related products in the repo space to transition to a sustainable economy.

While global regulators are seeking to implement global standards in this ESG arena, says Lees, it remains that lenders employ a highly diversified approach to ESG and securities lending. BBH works alongside their clients to implement custom solutions in an effort to tackle the differing sustainable priorities between clients. This means adhering to each client's governance requirements around restricting and recalling securities, while providing data around potential revenue that, along with governance policies, allows for optimal decision making.

Supporting this sentiment, Squillacioti adds that there is a lack of consistency across firms, with each client applying their own unique ESG criteria. This complexity requires bespoke ESG collateral schedules for each individual client. As a result they are not included in the omnibus pool — potentially, impacting their lending revenue potential.

Squillacioti remarks: "Work continues on several fronts to facilitate these differences among clients on internal non-cash collateral allocation methodologies, including with triparty banks to create flexible bespoke collateral schedules, and looking at industry ESG-scoring methodologies to attempt to create collateral sets that can gain wider client adoption."

Transparency is critical to the evolution of the ESG landscape as well as the management of ESG risk and regulatory compliance, highlights BNY Mellon's managing director and global head of securities finance Bill Kelly.

To help guide clients in operating ESG, BNY Mellon has released an ESG transparency dashboard which incorporates MSCI ESG ratings, assigning ESG scores to securities across environmental, social and governance. It can be applied to a client's non-cash collateral and cash reinvestment, including outright purchases and repo collateral. The dashboard helps to enable clients to analyse how their portfolio, the collateral they receive and the investments they make align to their ESG principles and policies.

Big steps forward

Enhancing post-trade processes, supporting clearing of securities lending trades, and expanding electronic trading looks to be the largest advances relating to technology development for 2023.

Working within the sales team at HQLA^X, Charlie Amesbury explains that a "big step forward" for development will be seen in the post-trade aspect of the securities finance industry, where firms will move from initial production trades into a full-scale volume on some of the market's digital platforms. He adds: "After a number of years of building out the legal framework, digital representations of traditional assets are poised to enter mainstream use, allowing the frictionless exchange of ownership which will ease pain points in the industry."

Similarly, enhancing post-trade processes will be a priority for State Street, who will continue to work with several vendors on this project for the next 24 months. Squillacioti explains that trade execution investment and technology has tended to garner the most attention in the past, but given the focus on transparency from a regulatory perspective, and efficiency from a commercial one, "it has pivoted the market to focus on the complete lifecycle of a trade holistically".

Wematch's co-founder and head of EMEA David Raccat says he has observed a huge need in post-trade and standardisation on the securities financing synthetic markets. The industry continues to push for advances in collateral management solutions, term sheet standardisation, workflow tools, and more efficient communication between sales and traders.

In general, securities finance continues to follow the direction of travel from other asset classes, explains Martin Walker, head of product, securities finance and collateral management at Broadridge. Over the last decade, the increased clearing of trades and electronic trading seen by the industry has massively reduced the number of post-trade exceptions and driven increased efficiency. However, the importance and volume of trade lifecycle events in securities finance does make it qualitatively different, Walker says.

BBH has seen a "significant" rise in trading automation across all fee spaces in 2022. This comes as a result of increased quantitative trading, reduced industry fail tolerance due to CSDR, and strict regulation in markets such as Korea. Lees expects this trend towards automated loan execution in higher fee loans to continue, in addition to the emergence of an increased number of automated routes to market.

Consequently, BBH indicates that investment in automated execution capability will be a key component of its investment strategy in 2023. Lees explains: "As loan execution becomes increasingly automated, the migration of complex trading strategies to code has become a key source of competitive advantage. Increased trading model complexity has yielded impressive results and BBH plans further investments in trading models, including the potential application of artificial intelligence in 2023."

During 2023, HQLA^X will continue to develop its agency securities lending delivery-versus-delivery (DVD) product, which aims to eliminate the intraday credit exposure inherent in this trade flow, bringing efficiencies for the borrowers, while allowing the lenders to offer post-trade technology solutions.

HQLA^X will also collaborate with industry members to introduce an intraday delivery-versus-payment repo capability through cross-blockchain execution between the firm and partnering digital platforms. "Our clients would have the ability to monetise their digital collateral records versus tokenised cash," says Amesbury. "This allows the borrowers more control over their intra-day liquidity, while lenders benefit from a new market in which to monetise their excess cash."

Following the launch of the Automated Trading Locates Allocation System (ATLAS), Clear Street plans to roll out ATLAS to European Markets in 2023. The system allocates stock loan inventory to incoming customer requests. Additionally, Clear Street is introducing a multi-asset and multi-market inventory and contract management system in the first half of 2023 that looks to improve the efficiency of the firm's securities finance desk. "It is all part of our plan to modernise the market infrastructure across capital markets, and improve market access for all participants," concludes Subbu.

The good and the bad

Raccat indicates that not only will the securities finance market need to adjust to an environment of higher interest rates, but also reduced central bank involvement in funding markets in 2023. He suggests that this will encourage the need to diversify funding sources and optimise balance sheet efficiencies, as funding costs increase.

Speaking to SFT on his predictions for loan supply and borrower demand, Squillacioti warns that RWA will remain a binding constraint for many borrowers and lenders across the market. He continues: "In 2022 we saw a noticeable increase in lendable supply with minimum spreads assigned, and can only assume that trend continues to grow next year."

This is expected to make it increasingly difficult for prime brokers to maintain legacy GC pricing, or, at a minimum, participants will see the count of securities available at GC decrease. He concludes: "In one form or another, this will likely result in higher borrow fees for prime brokers and ultimately for the end user."

According to Walker, the Basel III and Basel IV rules regarding unrated parties could lead to a significant reduction of supply for a number of years as countries adopt the standards. Increased RWA charges are expected to cause a larger impact in the general collateral (GC) market — where trades with unrated lenders are likely to become uneconomic.

"We have to remember that the long-term trend over a decade has been forever more supply of stock to be made available," suggests Walker. "Supply that the securities finance market has not been able to make full use of. The reduction in excess supply, particularly in the GC [market], would take some of the edge off the potential liquidity squeeze."

Despite these concerns, it is not all doom and gloom. Subbu predicts that central clearing models will unlock significant liquidity in 2023 and beyond. The Depository Trust & Clearing Corporation's (DTCC's) securities financing transaction (SFT) initiative, in particular, is expected to contribute to this, he says. The service aims to support the central clearing of SFTs between National Securities Clearing Corporation (NSCC) full-service members, as well as the central clearing of clients' SFTs intermediated by sponsoring members or agent clearing members.

Transaction costs are coming down, thanks to the advent of central clearing and the continued commodification of the lending process, Subbu highlights. As a result, an increasing number of beneficial owners are willing to participate in securities lending, thereby increasing supply.

Bringing to bear

As the industry takes its first steps into the new year, expansion seems to be a common theme for market participants who spoke to SFT.

Regulatory change is still a main focus and a major part of Broadridge's work. However, now post-SFTR and post-CSDR, the firm anticipates working with its user base on revenue generation and efficiency focused system enhancements.

Likewise, HQLA^{X} will continue to prioritise launching scalable solutions that will service their clients, as well as expanding their customer base. Amesbury indicates: "The collaborative work we are doing with other digital registries and technology providers remains a key focus, with the goal of creating an interoperable network in which the ownership of different asset classes located around the world can be exchanged seamlessly and efficiently."

Summarising State Streets' key focus for 2023, Squillacioti says the firm is looking to expand the business and client footprint in an "accretive and efficient manner", across all State Street businesses, while bringing to bear for each client the full suite of services that its financing solutions group offers.

Speaking to SFT, Subbu explains: "In May 2022, Clear Street raised US$165 million in our Series B funding round to further our mission to create a single-source platform to serve all investor types, across all asset classes, globally. Next year, we'll continue that work." Clear Street will focus on further expanding into Europe. In addition to building out its securities lending platform, the firm will focus on expanding and diversifying the securities lending supply so it can improve access to liquidity for customers.

The priority for the industry should be to continue to attract diverse talent to help drive innovation to meet the challenges and opportunities ahead, says Lees. He states that the Women in Securities Finance community has been "tremendously successful" in supporting diversity, equity and inclusion in the industry and BBH is committed to its further growth.

More specifically to BBH, the firm continues to focus on preserving its differentiated offering in the marketplace by investing in technology and client service. Lees concludes: "Securities lending is increasingly relevant for investors globally, and we are seeing the need for further customisation coupled with a desire from asset lenders to enhance transparency, optimisation and control."

Initial Margin: is it over?

The quest for efficiency and optimisation does not stop with the final UMR implementation phase, according to BNP Paribas' David Beatrix. For firms with a compliance process in place, careful monitoring is necessary to ensure everything is running properly. For firms that have not yet been impacted, they could be in the future

Initial margin rules for non-cleared derivative transactions have been progressively entering into force since 1 September 2016, released through a phased implementation with an increasing number of market participants subject to their requirements every year.

Phase 6 of the Uncleared Margin Rules was implemented in September 2022 and this has impacted a significant number of firms, including institutional investors. With this last wave now behind us, are we done with initial margin concerns?

Reminder on the initial margin rules

Exchanging initial margin (IM) on non-cleared derivative trades has become an established practice over the years. Now that we are past the final phase, all firms with an Aggregate Average Notional Amount (AANA) of non-centrally cleared derivatives (at consolidated group level) above €8 billion are subject to IM rules. All instruments — even physically settled forex forward and forex swap transactions that are exempted from IM requirements — count for the purpose of calculating the AANA.

Most financial counterparties trading non-cleared derivatives are “in-scope” and exemptions are very limited. As of today, the rules have been transposed in a number of jurisdictions (including the European Union, US, Japan, Australia, Hong Kong, Singapore). In many jurisdictions where the rules have been implemented, the treatment of third-country entities implies that most cross-border transactions entered into with entities incorporated in third-country jurisdictions are in-scope.

The range of non-cleared derivative instruments falling into scope of the regulation — that are subject to collection of IM — is generally consistent across the main jurisdictions in Europe, Asia Pacific and the US. Physically settled forex forwards and swaps are excluded across all jurisdictions.

However, some jurisdictions may have specific exemptions, either on a permanent basis (e.g. equity options and forwards are out of scope in the US) or on a temporary basis (e.g. equity options are exempted in the EU until January 2024).

IM rules have many specificities owing to the method for calculating IM amounts, the principle of bilateral exchange of margin (each party posts and receives at the same time), the possible relief with the €50 million threshold, and custodial segregation aspects. The compliance process is complex and can take from six to nine months on average. To manage these requirements, firms have different options to ensure compliance — whether implementing the rules by their own means, or appointing a service provider that can offer an end-to-end solution.

Staying alert

Although the final phase has passed, vigilance must endure.

For firms with a compliance process already in place, solid monitoring is necessary to ensure everything is running properly. Moreover, the quest for efficiency and optimisation does not stop. As IM exchanges take place and data is recorded, the market will be able to reflect and develop further efficiencies to ensure a smoother IM compliance process.

Additionally, there are firms that have not yet been impacted, but could be in the future. There are two main things for these firms to consider:

1. their Aggregate Average Notional Amount (AANA) and how to track its evolution. Approaching the €8 billion threshold should instantly trigger consideration of IM requirements and how to respond to them.
2. the relief mechanism linked to the €50 million threshold instituted by the Basel Committee on Banking Standards (BCBS), which we explore in more detail below.

Finally, the rules may change over time. As we observe reviews of other major regulations, we note that public consultations have recently taken place around the IM model validation framework for example. Some updates may arise in the short- to medium-term.

Buying more time

The relief mechanism has been introduced to take into consideration the differing levels of risk represented by different volumes of uncleared OTC derivatives trades. BCBS states:

“The requirements could impose some unnecessary operational costs on smaller entities that pose no significant systemic risk to the system and would not be expected to be bound by the initial margin requirements, in particular, in light of the provided threshold amount of €50 million.” (BCBS, Margin requirements for non-centrally cleared derivatives, April 2020)

As always, the devil is in the detail: this €50 million threshold is the maximum threshold a firm can set at consolidated group level with another trading relationship. For institutions having multiple entities, themselves in trading relationships with several branches of a bank, a significant part of the preparatory work is to map and allocate the appropriate threshold amount to each relationship, the function of the expected trading activity post-compliance date and the risk profile of the transactions. Finally, for the same relationship, it could also happen that these thresholds have been set in an asymmetric way between the pledger and pledgee directions.

If, for a given trading relationship, the uncleared OTC derivatives portfolio (“in-scope” — that is, having all of its trades executed after compliance date) has its IM amounts under the thresholds (€50 million or lower, depending on the allocation mechanism described previously), it is then exempt from posting IM until it reaches this threshold. Firms falling below the threshold are not expected to have specific documentation, custodial or operational processes related to IM in place. This, however, is only supposed to grant more time for firms to prepare for full IM compliance. Once this threshold is exceeded, firms are expected to have all necessary processes in place and operational.

Relying on the threshold requires precise monitoring. To this end, firms can rely on providers that offer such services. At BNP Paribas, we have developed a threshold monitoring service to accurately monitor that the IM threshold is not breached. This solution gives clients additional time to prepare for full IM compliance and allows them to keep trading even though their IM framework is not fully in place.

We offer threshold monitoring services in two ways:

- via our own IM management system, relying on clients’ portfolio data.
- through Acadia’s IM Threshold Monitoring module, relying on counterparties’ data.

This is offered alongside a full suite of IM services, including IM calculation, exposure management and pledge management via our triparty collateral service.

IM will also remain an area of focus on our side going forward. As a service provider, we continue to look for ways to further improve the quality of IM services for our clients.

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A fruitful 2022 for securities finance markets

S&P Global Market Intelligence's director of securities finance, Matthew Chessum, and director for beneficial owner services, Rob Nunn, review securities lending market revenues during 2022 and provide pointers for expected market performance into 2023

The securities finance markets have had a lot to be thankful for in 2022. The emergence of geopolitical risk and increased levels of volatility have reawakened short sellers and have collectively created the perfect conditions for securities finance revenues to reach highs not seen since 2008. Many asset classes beat their full year 2021 revenues in November with some, such as corporate bonds, as much as 60 per cent higher.

Throughout 2022 there were four stand out asset classes that outperformed when compared to recent years: US equities, ETFs, corporate bonds and government bonds.

Americas equities

Securities finance revenues generated by Americas equities increased steadily over the year, generating US$4.4 billion by the end of November. Several well-documented borrows have provided strong revenues for lenders throughout the year and most of the specials activity that took place in the equities markets can be attributed to Americas equities.

The first three quarters of 2022 generated more lending revenues from Americas specials than all four quarters of any other recent year.

At the time of writing, the top revenue-generating stocks of 2022 are all Americas equities. Top specials of 2022 include Lucid Group (LCID) generating US$263 million to 15 December, Gamestop (GME) generating US$227 million to 15 December, and Beyond Meat (BYND) generating US$184.6 million.

Exchange-traded funds

ETFs benefited from the hawkish interest rate environment throughout 2022, with high yield and investment grade trackers seeing strong demand. The fall in corporate bond prices provided opportunities for both hedging and directional borrowing through ETFs. HYG (iShares iBoxx HY bond ETF) had generated US$109 million in revenues for lenders through to 15 December for example.

Other popular borrows that helped to push securities finance revenues higher were small and mid cap trackers such as IWM (iShares Russell 2000 tracker), which generated US$29.4 million for January to November.

ETFs that permit offshore investors to participate in operationally challenging markets such as CNYA (iShares MSCI China A shares) generated US$14.2 million (for January to November) and EWZ (iShares MSCI Brazil) also generated steady revenue flows of US$7.6 million (January to November). Americas ETFs dominated the ETF borrow market during 2022. Through the end of November, 86 per cent of all collective ETF revenues were attributable to Americas ETFs.

Corporate bonds

Corporate bonds became more expensive to borrow during 2022. Average fees climbed throughout the year, starting 2022 at an average of 29bps and finishing November at an average of 41bps. On-loan balances also increased significantly when compared to previous years. 2022 has been one of the best-performing years for corporate bonds on record and demand has remained widespread throughout the year. Specials have existed but demand for the asset class, as noted by a rapid increase in on-loan balances, has not been limited to specific bond issues. As interest rates continue to ratchet higher, pressure is likely to remain on corporate bond prices, providing further opportunities for both long and short investors in this asset class in 2023.

Government bonds

Government bonds remained attractive to borrowers throughout 2022. A general flight to quality, and the introduction of the final phase of the Uncleared Margin Rules (UMR) in Europe, all contributed to strong demand. Revenues increased steadily over the year, with only January failing to beat the same month in the previous year. By the end of November, revenues were 103 per cent of those generated throughout the whole of 2021.

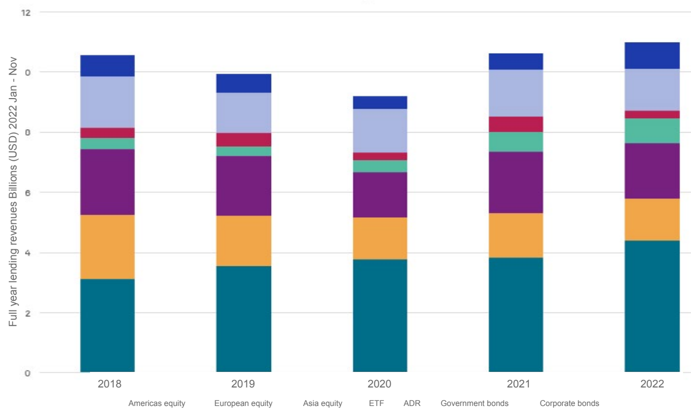
Rob Nunn points out that despite 2022 being a strong year for the market-wide revenues, not all lenders have benefited from this trend. He indicates that if you held a broad range of US equities, ETFs and corporate bonds, you have probably had a good year. In contrast, if your asset pool is more concentrated, which is more the norm during times of heightened volatility, your revenues may not be reflective of those experienced by the broader market.

According to Nunn, global regulatory restrictions can also have a significant impact on the revenue generated from securities lending programmes. Regulations surrounding how UCITs funds or US 40 ACT funds can participate in securities lending activities, for example, can sometimes be restrictive if they are not fully understood or effectively managed.

As investment managers act as responsible stewards of client assets, independent oversight management of delegated functions, such as securities lending, is recommended by global regulators. It is important to understand the flexibility that beneficial owners have within regulatory obligations to optimise their returns, but also what data and tools are available to help to understand and manage a programme's risk profile.

Several other factors can also impact a beneficial owner's ability to generate revenues. These include regulation, collateral types (for example, cash, equities, government bonds, corporate bonds, ETFs), collateral transmission (pledge collateral versus title transfer), levels of margin, counterparty lists, trade durations, agent lender operational structures, as well as any minimum fee and recall policies.

Figure 1: Securities lending revenues (USD)



At S&P Global, we have developed numerous solutions to help manage securities lending programmes. These are designed to enhance transparency and build trust with stakeholders. This, in turn, ensures that securities lending is operating in the best interests of all parties. The solutions on offer help stakeholders to work proactively with their lending agents to enhance and improve performance, optimise and monetise new opportunities, effectively manage the liquidity profile of a programme's assets, and help to improve risk management.

As we head into 2023, the securities finance markets are likely to continue to be driven by both inflationary and recessionary factors. Both fiscal and monetary policy will remain central to market movements as governments decide whether growth or deflation is the main driver of economic policy. As in 2022, the securities finance market is well positioned to take advantage of current economic trends and is expected to continue to generate important returns for all investors throughout 2023 no matter what side of the market they belong to.

Latest industry moves at OCC, Sharegain and State Street

The Options Clearing Corporation (OCC) appoints Dan Busby as its new chief operating officer after Scot Warren announces retirement.

Currently acting as chief administrative officer, Busby will step into his new role on 1 January 2023.

Busby is a 23-year veteran at OCC and previously served as chief clearing and settlement services officer.

Prior to this, he held leadership roles in internet and investor services, member services and business operations.

He succeeds Warren, who will remain in his current position as COO until 2023, when Warren is set to retire from the organisation after seven years of service.

OCC has also announced the appointment of Mike Hansen to chief clearing and settlement services officer from 1 January 2023.

Hansen currently acts as managing director of clearing and settlement operations and will soon join OCC's management committee, once his new role takes effect.

Hansen has more than 20 years of options industry experience and has served in various roles throughout his tenure at OCC including back-office processing, pricing and member services.

OCC executive chairman Craig Donohue thanks Warren for his contributions to the organisation. Since joining the company in 2015, Warren has been instrumental in driving OCC transformation, creating alignment across the enterprise and enhancing the execution of OCC's strategic vision and corporate goals.

Securities industry veteran Yawar Shah will leave the Swift board of directors after 16 years as chair.

Mark Buitenhek, currently deputy chair of the board, will fulfil the responsibilities of the chair until a new chairperson is elected by the Swift board of directors in coming months.

Shah is managing director in the institutional clients group at Citi, having worked at the New York-based bank since 2007.

Prior to this, he was executive vice president at J.P. Morgan, serving at J.P. Morgan from 1987 to 2007.

State Street hires Allen

State Street has appointed Nancy Allen as assistant vice president for the EMEA financing solutions business development team.

The team is responsible for the sales of State Street's lending, prime brokerage and repo solutions.

Based in London, Allen will report to EMEA head of financing and collateral business development solutions, Cassandra Jones.

She joins the firm from UBS, where she was previously a prime brokerage sales assistant from 2019 to 2022.

Prior to this, Allen held work experience within State Street's securities finance team within the agency lending division in 2018.

Commenting on his time on the Swift board, Yawar Shah says: "It has been an honour and privilege to serve the global financial community as chair of Swift and as a representative of the US community on the Swift board.

"I am immensely proud of the cooperative's many achievements in transforming the cross-border experience for both payments and securities, while upholding the highest levels of security, resilience and reliability."

SWIFT CEO Javier Pérez-Tasso adds: "I would like to recognise Yawar's many contributions to the Swift community over the years. I look forward to working together with the board through the leadership transition as we continue to deliver on our global vision for instant and frictionless transactions with the highest standards of operational excellence."

In closing, Shah indicates that Swift is "in great shape" with strong financials, growing traffic, industry momentum around its strategy and exciting innovation ahead.

"At the end of a successful year, and as we move to the next phase of strategic delivery, it is the right time for me to retire from the role of chair and the board," he says.

Shah adds: "I would like to thank Swift board colleagues from around the world for their continuing dedication and together with Swift's management team, I am confident the cooperative remains in excellent shape for the years ahead."

Sharegain appoints Finkel

Sharegain, a securities lending and capital markets infrastructure fintech, has appointed Ahikam Finkel as vice president of research and development (R&D).

Finkel brings experience in scaling and globalising R&D teams to the role, which will see him scale Sharegain's R&D capabilities with the intention to turn it into a global capital markets' R&D powerhouse.

He joins the firm from app measurement and analytics company AppsFlyer, where he was previously vice president of research and development operations.

In this role, Finkel managed the cross R&D processes as AppsFlyer grew from 70 to more than 400 engineers.

With 20 years of experience in a variety of R&D and leadership roles, Finkel was previously R&D scaling consultant for various Israeli technology companies and R&D, automation and quality assurance leadership roles at Jethro, Sigma Designs and Expand Networks.

Toronto-based bank Scotiabank has appointed Amandine Triadu as director, head of collateral management and funding for Europe and Asia.

Based in London, Triadu will report to Robert Dias, managing director and global head of collateral management and funding.

She will report locally to Gabriel Buteler, head of fixed income, currencies and commodities (FICC) sales and trading for Europe and Asia, and global head of rates trading.

Triadu joins the bank after acting as head of repo trading for EMEA at Mizuho from 2019 to 2022.

Prior to this, Triadu was employed by Nomura International where she held a position as covered bonds and credit (DM) repo trader from 2012 to 2019.

This position followed a similar role she held previously at BNP Paribas Fortis, where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Triadu was covered bonds and credit (EM/DM) repo trader.

Financial services company Mizuho has promoted Vivek Patel as head of repo trading.

Based in London, Patel enters the position as the firm looks to expand its repo capability across the banking and securities units in Europe, the Middle East and Africa.

Prior to joining Mizuho in August 2020, Patel was positioned at HSBC Global Banking and Markets as an associate between 2016 and 2020.

Previously, he held an analyst position at Bank of America Merrill Lynch.

BNY Mellon has appointed former Aviva Investors head of securities finance Ben Meaden as director of securities finance.

Based in the UK, Meaden will report to Simon Tomlinson, global head of securities finance trading.

The appointment follows the decision by Aviva Investors to move its securities finance team to BNY Mellon.

He takes on the role after almost 20 years at Aviva Investors, where he was most recently head of securities finance.

Meaden joined Aviva Investors in 2003 as a desk assistant before becoming a securities finance trader in 2005, where he handled securities lending, repo and funding transactions.

He was later promoted to head of trading for securities finance prior to entering his latest role. Previously, Meaden worked within collateral management at Maple Securities in 2003.

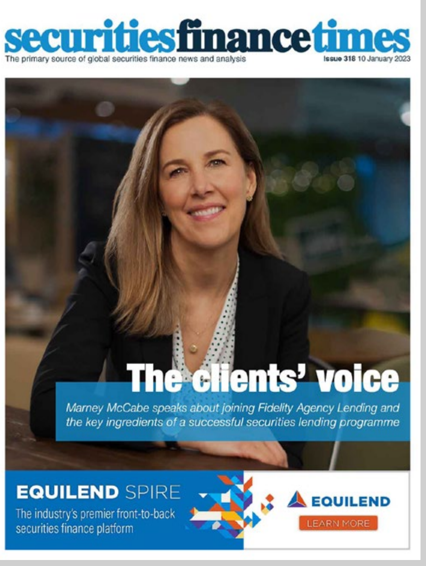
In September, Aviva confirmed that it had appointed BNY Mellon to provide an integrated operating model for middle and back office, along with selected front-office support services.

This forms part of a broader asset servicing solution, through which BNY will offer custody, fund administration and depository services, alongside front-office solutions including performance measurement and mandate monitoring. Among other benefits, this will extend the advantages of BNY Mellon cloud-based data platform, Data Vault, to support Aviva's investment activities.

Speaking at the time of this announcement, Aviva Investors' CEO Mark Versey explained that Aviva had entered into an asset-servicing partnership arrangement with BNY Mellon as part of the efforts to streamline its supplier model and to deliver a "best-in-class, scalable operating model for the benefits of our business and clients".

"Outsourcing some of these services to BNY Mellon will allow us to enhance our client proposition and improve operational efficiency," Versey explained.

Roman Regelman, CEO of Securities Services and Digital at BNY Mellon, commented: "Our innovative, data-centric operating model, flexible technology and comprehensive capabilities will enable Aviva Investors to focus on delivering an exceptional client experience. We are delighted to support Aviva Investors on its journey to transform its operating model."



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