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Goldman Sachs settles charges of short selling violations in the US

Goldman Sachs has agreed to pay $15 million to settle charges of improper securities lending practices that violated federal regulations.

The bank's broker-dealer was accused of violating Rule 203(b)(1) of Regulation SHO and Section 17(a) of the Securities Exchange Act by improperly providing locates for short selling purposes to customers where it had not performed an adequate review of the securities to be located.

Goldman Sachs did not admit or deny the accusations brought against it.

Goldman Sachs instead consented to the cease and desist order and agreed to pay the $15 million penalty.

"The requirement that firms locate securities before effecting short sales is an important safeguard against illegal short selling," said Andrew Ceresney, director of the Securities and Exchange Commission's (SEC) enforcement division. "Goldman Sachs failed to meet its obligations by allowing customers to engage in short selling without determining whether the securities could reasonably be borrowed at settlement."

Andrew Calamari, director of the SEC's New York regional office, added: "SEC exams ensure that market participants are following the rules, so there will be consequences, including in the determination of remedies, when a registrant fails to provide complete and clear responses to examination staff."

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SFTR now up and running

New European rules demanding greater transparency and more comprehensive reporting requirements for securities financing transactions (SFTs) came in to effect on 12 January.

The Securities Financing Transactions Regulation (SFTR) ((EU) 2015/2365), published in the Official Journal of the EU, creates a framework under which details of SFTs can be more efficiently reported to trade repositories.

The guidelines also introduce new collateral management conditions.

The three main features include the mandatory reporting for all SFTs, excluding those concluded with central banks, to trade repositories.

Reporting requirements will be implemented at a regional level between 12 and 21 months after the SFTR came into force on 12 January.

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ESMA short with national securities regulators

Only one in five EU national regulators is fully compliant with the Short Selling Regulation, according to a peer review by the European Securities and Markets Authority (ESMA).

ESMA's review of the financial services regulators in the UK, Germany, Italy, Sweden and Hungary found multiple inconstancies in the regulation's application.

Specifically, ESMA scrutinised the discrepancies in the regulators' application of the exemption for market making activities in Article 17 of the Short Selling Regulation.

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Goldman Sachs settles charges of short selling violations in the US

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The SEC found that the locates were inaccurately recorded in the bank's locate log, which must reflect the basis upon which Goldman Sachs has given out locates.

Members of the bank's securities lending demand team routinely processed customer locate requests by relying on a function of the Goldman Sachs order management system known as 'fill from auto-locate', which was accessed via the 'F3' key, according to the SEC.

This function caused the system to grant locate requests based on the amount of reliable start-of-day inventory reported to Goldman Sachs by large financial institutions, even though its automated system had already deemed this inventory to be depleted based on locate requests processed earlier in the day.

When Goldman Sachs employees used this function to grant locate requests, they relied on their general belief that the automated model was conservative and the granting of additional locates would not result in failures to deliver when the securities became due for settlement.

In doing so, the Goldman Sachs employees did not check alternative sources of inventory or perform the necessary reviews of the securities to be located.

Goldman Sachs's documentation of its compliance with Regulation SHO was also inaccurate as it failed to sufficiently differentiate between the locates filled by its automated model and those filled by the demand team using the fill from auto-locate function.

In both cases, the locate log simply mentioned the term 'auto-locate' to refer to the start-of-day inventory utilised by the bank's automated model as the source of securities underlying the grant of a locate.

The US regulator accused Goldman Sachs of providing "incomplete and unclear responses that adversely affected and unnecessarily prolonged the examination", during a review into its securities lending practices in 2013.

Goldman Sachs did not respond to a request for comment on the settlement with the SEC.

SFTR now up and running

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Investment funds must also disclose information on the use of SFTs and total return swaps to investors in their regular reports and in their pre-contractual documents.

This rule came in to immediate effect with the SFTR but existing funds will receive an 18-month grace period to amend their books.

Finally, the SFTR sets minimum transparency conditions on the reuse of collateral. Disclosure of risks and the need to grant prior consent are just some examples of what the new regulation entails.

The collateral management conditions will come into force six months after the launch of SFTR.

The new regulation comes in response to claims that the extensive reform of the traditional banking sector, without equivalent rules for shadow banking entities, would drive business towards these less regulated areas and subsequently cause a less transparent environment than before the crash.

Both financial and non-financial entities will be affected by the new requirements.

Transactions with members of the European System of Central Banks are

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exempt from the obligation to report SFTs to trade repositories.

ESMA short with national regulators

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The assessment group concluded that, of the five regulators reviewed, only the Italian Securities and Exchange Commission is fully compliant with ESMA guidelines.

The remaining four were deemed to be "partially non-compliant to differing degrees", according to ESMA's report.

Exempted market makers are not subject to the restrictions on uncovered short sales.

They are also not subject to the reporting and public disclosure obligations of significant net short positions in shares or sovereign debt.

ESMA raised concerns that the regulators are not properly seeking assurance in advance that market makers comply with organisational requirements.

All of the regulators except Italy's were found to be applying a 'per firm' approach to processing notifications for exemptions rather than a review of the notifications instrument by instrument, which is required by the guidelines.

Many national regulators place an over-reliance on monitoring by trading venues, instead of monitoring themselves to check compliance, according to ESMA.

"Different interpretations of the short selling regulations persist resulting in different practices among national conduct authorities (NCAs)," stated ESMA.

This is an unsatisfactory state of affairs and should be clarified when the Short Selling Regulation is being reviewed."

"The differences of opinion on the application of the Short Selling Regulation between ESMA's guidelines and the practices of some NCAs need to be resolved, since the different implementation of the guidelines at [EU] level is far from ideal."

ESMA has since submitted the report to the European Commission, which will now clarify how the Short Selling Regulation should be interpreted going forward.

The authority also aims to streamline the definition of market making as part of its upcoming review of the regulation, as this contributes to some of the divergent supervisory practices among national regulators.

Stanbic IBTC launches Nigerian securities lending programme

Stanbic IBTC Bank has launched a securities lending product in Nigeria.

The bank will become one of the first registered securities lending agents (SLAs) to operate through Nigeria's Central Securities Clearing System's (CSCS) securities lending facility, which launched in September 2015.

The launch marks the latest of several new products to be introduced to the Nigerian market, including the Purchasing Manager's Index, a composite index for measuring private sector activities to provide an early indication of business conditions in the country.

Stanbic IBTC Bank also launched the Stanbic IBTC Exchange-Traded Fund 30, an index built on the NSE 30 Index, which tracks the 30 most capitalised companies on the Nigerian Stock Exchange.

Yinka Sanni, CEO of Stanbic IBTC Bank, said: "As a member of a global banking group, Stanbic IBTC has a responsibility to help

grow the capital market through products and initiatives that could help investors harness investment opportunities that exist in Nigeria."

"We are delighted to be introducing the Stanbic IBTC securities lending product into the Nigerian market. The product launch is a further demonstration of our commitment to facilitating stability and growth of the Nigerian capital market, via confidence building initiatives and leveraging investment opportunities in the market. Other derivatives will be introduced in the future."

Oscar Onyema, CEO of the Nigerian Stock Exchange, noted that various initiatives have been introduced to strengthen the capital market, including derivatives.

He described the investment opportunities in the capital market and Nigeria's economy as "huge".

Onyema said: "Despite the prevailing challenging operating environment and the attendant indifferent performance of the capital market, characterised by low level investor confidence, there still exists enormous investment opportunities for Nigerians to leverage."

It's not all bad news in the Chinese markets

The market sell-off in China has led to a spike in short-term repo rates but, in the long term, "fundamental reform" is required to turn the jurisdiction's fortunes around, according to Gary Greenberg, head of emerging markets and lead portfolio manager at Hermes Investment Management.

He also suggested, however, that 2016 is the year to establish a position in emerging markets such as China.

Chinese markets have continued to fall, said Greenberg, but the government's withdrawal of liquidity has led to an increase in short-term repo rates.

The stock market, however, has dipped by 5.3 percent.

As 'circuit breakers' were withdrawn, there was no opportunity for the kind of selling that has intervened in the past.

Greenberg said: "Most interestingly, [head of the state council] Li Keqiang ruled out strong stimulus to boost demand. This supports the move to supply-side economics proposed by [China] President Xi Jinping."

In the long term, significant changes will be essential to a successful future, and that means, "increasing efficiency and productivity rather than mobilising yet more capital".

While China's growth model will have to adapt, it will be difficult to change the drivers of the economy, and there is some doubt over whether authorities can make the changes without falling in to a crisis.

Greenburg said: "How can an economy, in which investment is nearly 50 percent of GDP and consumption less than 40 percent, evolve to one in which consumption is over 60 percent of GDP and investment under 30 percent, in several years?"

This is further complicated by the dominance of retail investors in domestic Chinese markets—investors that have short-term horizons and few tools for valuing stocks, and that follow momentum of price shares, earnings, or economic policy. "Therefore, when the government hints at stimulus, regardless of whether or not stimulus will result in better long-term prospects for the country (and it is unlikely to, given its debt-to-GDP ratio is nearing 300 percent), retail investors plunge in."

Greenburg added: "On the other hand, when reforms are put forward these investors sell, since reforms spell short-term pain as excess capacity is cut."

Institutional investors are more likely to make short-term sacrifices for long-term gains, explained Greenberg.

He added: "In contrast, Chinese stock markets gyrate wildly at such a crossroad."

According to Greenberg, developed markets are outperforming emerging markets because of underperformance on the bottom line in emerging markets. As global growth has slowed, so too has profitability.

He suggested that emerging markets may appear to offer a cheap investment with a low benchmark, but as profitability suffers, the price-to-earnings ratio is less appealing.

But improving the picture for China may not be easy. Greenberg said: "A brighter outlook will probably require some combination of lower valuations, currency depreciation of 5 to 10 percent, a change in the trend of US dollar strength, a bottoming of commodities markets, stabilisation of the RMB and local markets, and for corporate margins to improve."

He predicted that stabilisation of commodities and margins will begin in 2016, become more evident in 2017, and become a theme in 2018.

"Therefore, this year is the one in which to initiate a position in emerging markets, before building a strong overweight next year ahead of enjoying the ride in 2018."

Greenberg concluded: "Periods of panic, such as now, are typically good times to look for stock ideas."

"While the valuation of the benchmark is not yet compelling on all measures, this type of market results in the mispricing of companies, which can provide real long-term opportunities."

HCMC rejects ESMA's rejection

Greece's Hellenic Capital Market Commission (HCMC) has disregarded the European Securities and Markets Authority's (ESMA) disapproval of its renewal of the short selling ban.

The Greek and European regulators disagreed on the need to continue the prohibition of shorting shares of Attica Bank.

The ban, which has been ongoing since June 2015, expired at midnight on 11 January but was reinstated until 25 January.

It includes all sales of Attica Bank shares covered by subsequent intra-day purchases.

It also applied to all depository receipts and warrants representing the bank's shares admitted to trading on the Athens Exchange.

Market makers will continue to be exempt from the ban.

HCMC, in its explanation for extending the ban, said that Attica Bank, as the last Greek bank to be re-capitialised, should also be protected from short selling in the same way as other banks were.

The delivery of beneficiaries' new shares isn't finished and the date of admission to trading of the new shares has also not been confirmed. Therefore, in the interest of consistency and equal treatment, the ban was renewed, according to HCMC.

ESMA had previously endorsed all eight renewals of the ban since it was first proposed last year, citing "adverse developments that had constituted a serious threat to market confidence in the Greek market".

These conditions, according to ESMA, have now "considerably decreased with the successful completion of the share capital increase of Attica bank as announced by that bank on the 30th December 2015".

In a statement on its decision, ESMA said: "ESMA notes that the trading of the newly issued shares further to the completed capital increase has not started yet and thus there is a risk of increased volatility in the relevant market and that the confidence in the concerned bank could be affected if price movements were extreme."

Hedge fund performance down

SS&C GlobeOp's Hedge Fund Performance Index reported that gross returns fell by 0.34 percent in December 2015, an increase on the 0.21 percent decline seen in the previous month.

Hedge fund flows as measured by the SS&C GlobeOp Capital Movement Index also declined by 2.77 percent in January. This is down from a 0.75 percent advance in December.

The index represents the monthly net of hedge fund subscriptions and redemptions administered by SS&C GlobeOp on the SS&C GlobeOp platform.

The monthly net is divided by the total assets under administration for fund administration clients on the SS&C platform.

The Capital Movement Index stands at 143.44 points for January 2016, a decrease of 2.77 points over December 2015 and a decline of 2.81 points over the past 12 months.

"January typically sees the highest outflows of any month as investor rebalancing occurs," explained Bill Stone, chairman and CEO of SS&C Technologies.

"This seasonality can be seen in SS&C GlobeOp's Capital Movement Index for January 2016 which came in at -2.77 percent following a gain of 0.75 percent for December 2015."

"In terms of the year-over-year comparison, the -2.77 percent for January 2016 is an improvement over -3.28 percent for January 2015, a favourable result particularly in view of recent market turmoil."

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

Societe Generale launches SG CTA Mutual Fund Index

Societe Generale Prime Services has created its new SG Commodity Trading Advisor (CTA) Mutual Fund Index.

The latest offering, which went live on 1 January, will work as a performance benchmark for US '40 Act registered mutual funds that follow managed futures strategies.

The new index includes the 10 largest CTA mutual funds and is the fourth daily index designed and calculated by the French financial services provider.

The indices calculate the daily rate of return for an equally weighted group of the largest CTAs (by assets) that are open to new investment and provide daily data.

James Skeggs, global head of alternative investments consulting at Societe Generale Prime Services, said: "The '40 Act CTA mutual fund space has grown at an impressive pace, increasing more than five-fold in the last five years to exceed $22 billion in assets under management by the end of 2015."

"We are delighted to present the new index as a benchmark for the fast growing liquid alternatives CTA strategies. We welcome the 2016 SG CTA Mutual Fund Index constituents

and thank them for their help in the index launching process."

Kawada Capital upgrades

Kawada Capital Brokers has expanded its prime custody services to hedge fund clients of its prime brokerage business.

The firm now aims to provider both prime brokerage and global custody services through a fully integrated platform.

Building upon the recent launch of its enhanced prime brokerage offering, the prime custody service enables clients to segregate securities using a bank custodial account.

The platform utilises two Kawada Capital Brokers divisions: Kawada Capital Brokers Securities Services and Kawada Capital Brokers Prime Brokerage.

Kawada's integrated prime custody offering includes efficient movement of securities between custody and prime brokerage accounts, consolidated reporting, a single client-facing technology portal, as well as a dedicated client service representative supporting all products.

The services expansion was also complemented by the appointment of Mark Kozuki as CEO of the firm's securities services business.

Kozuki, who took on the role in December and will be based in Tokyo, is responsible for all aspects of the securities services business including sales, operations, technology, product, client service and the organisation's strategic agenda. Prior to joining Kawada Capital Brokers, Kozuki served as managing director and regional business head at a large investment bank. He managed the custody and clearing services, fund accounting and fund administration businesses.

Yao Chizuko, CEO and chairman of Kawada Capital Brokers, commented: "Mark Kozuki brings more than 20 years of financial services experience to his new role and will be an invaluable addition to the region. His appointment reflects Kawada Capital Brokers strong commitment to growing the worldwide securities services offering in the Southeast Asia region."

"We have a steadfast focus on our clients' continuing and evolving needs and with Mark Kozuki's experience and guidance we will continue to ensure that our clients have access to the full product and service power of the firm globally."

OneChicago had strong year

OneChicago achieved its third consecutive record year, chalking up 7 percent volume growth in 2015.

The exchange's volume especially took off in December, which was up 36 percent on last year's figure.

The December boost helped push OneChicago's total annual volume just over the 11.7 million mark.

Open interest increased 3 percent year-over-year to 662,876 contracts on the securities finance exchange at close-of-market on 31 December 2015.

Just over half of month-end open interest for December was in OCX.NoDivRisk products.

December GSF dip for Clearstream

Clearstream's global securities financing (GSF) services scored a monthly average


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outstanding of €542.1 billion in December 2015, but the figure was down on the previous year.

The post-trade infrastructure provider's triparty repo, securities lending and collateral management services collectively experienced a decrease of 14 percent over 2014.

The combined services achieved a monthly average outstanding of €627.6 billion in December 2014.

For 2015, the monthly average outstanding reached €598.6 billion compared to €609.8 billion in 2014, a decrease of 2 percent.

Markit's most shorted stocks ahead of earnings announcements

Fastenal, Suedzucker and Cave Interactive are among the most shorted companies ahead of upcoming earnings announcements, according to Markit.

The most shorted in North America was Fastenal with 15.9 percent of shares outstanding on loan.

Shares for the industrial and construction supplies company hit a year-low at the beginning of October 2015 but have subsequently rallied 12 percent.

This has attracted short sellers who have increased positions by 24 percent, ahead of earnings announcements.

The second most shorted in North America was biotechnology company MiMedx Group with 14.9 percent of shares outstanding on loan.

Although shares have faltered since July 2015, falling 26 percent in the past six months, some of this was recently recovered thanks to positive earnings guidance released by the company.

Suedzucker was once again the most shorted in Europe ahead of earnings at the start of the year.

Suedzucker currently has 2.5 percent of shares outstanding on loan, although share prices have risen 12 percent in the past three months.

This was driven by sugar prices finally bottoming out in 2015, according to Markit.

After several years of declining prices, a slight recovery was seen in the final months of the year despite the company recently guiding earnings expectations lower.

In the Asia Pacific region, the most shorted ahead of earnings was Japanese app and game developer Cave Interactive, with short interest jumping a third.

There are 10.8 percent of shares outstanding on loan with the stock moving higher by 68 percent in the past three months alone.

Eurex Repo volume down in 2015

Deutsche Börse Group subsidiary Eurex Repo's average outstanding volume for 2015 dropped by €26.7 billion compared to the previous year.

Eurex Repo's outstanding average for last year reached €172.8 billion, down from €199.5 billion in 2014.

The secured money market GC Pooling recorded an average outstanding volume of €140.9 billion in 2015, down from €158.5 billion.

The euro repo market as a whole reflects this negative growth as it totalled just €31.9 billion last year, down from €41 billion in 2014. Combined volume was €142.5 billion for December 2015, down slightly from €194.1 billion in December 2014.

Eurex's derivatives market bucked the trend for 2015 as its average daily volume reached 9.9 million contracts, an increase from 9.2 million the previous year.

OCC sees December securities lending boost

The Options Clearing Corporation's (OCC) securities lending central counterparty (CCP) activities saw a 19 percent increase in new loans in December 2015, compared to the same month in 2014.

The CCP recorded 138,358 securities lending transactions last month, compared to 116,240 in the same period in 2014.

Stock loan activity was up 16 percent in 2015 from the previous year with 1.3 million new loan transactions in 2015.

The average daily loan value at OCC in December was $155.79 million.

OCC also cleared 66.9 million futures contracts in 2015, a 1 percent decrease from 2014.

The corporation ended the year with seven million cleared futures contracts in December, up 15 percent from December 2014.

OCC's average daily cleared futures volume was down 1 percent in 2015 with 265,496 contracts.

Exchange-listed options volume was down 3 percent in 2015 with four billion contracts.

Total options volume in December was 338.8 million contracts, down 4 percent from December 2014.

Average daily options volume in 2015 was down 3 percent at 16 million contracts.

DATALEND

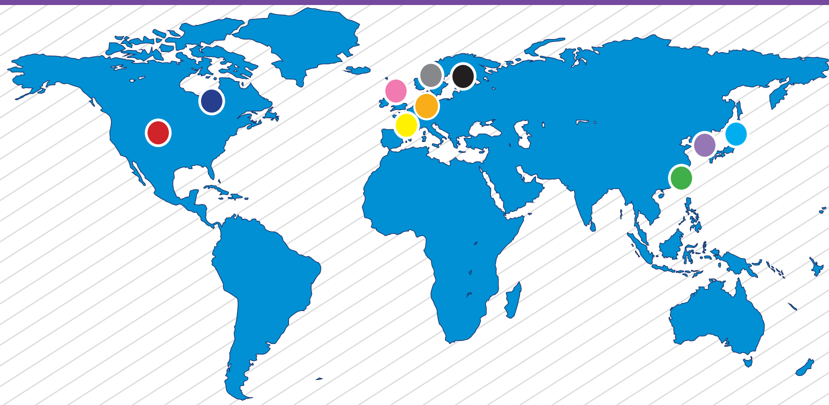
SECURITIES LENDING 2015 YEAR IN REVIEW

GROSS REVENUE | $8,611,345,310

North America: $4,211,053,544 Europe: $2,825,497,073 Asia: $1,446,794,076 Other: $128,000,616

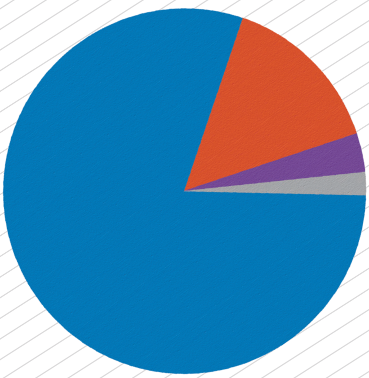
TOP 10 COUNTRIES BY GROSS REVENUE MILLIONS, USD EQUIV.

United States	$3,805
Germany	$632
France	$586
Hong Kong	$494
Canada	$406
Japan	$309
Great Britain	$282
Korea	$267
Sweden	$240
Finland	$110



AVERAGE ON LOAN BY ASSET CLASS BILLIONS, USD EQUIV.

FIXED INCOME



SOVEREIGN DEBT $672

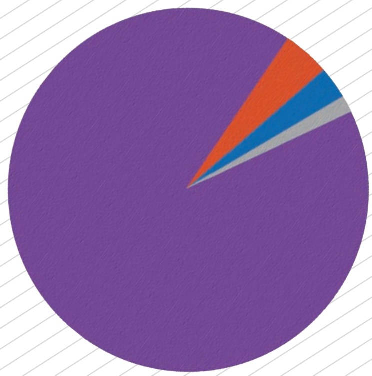
CORPORATE $117

AGENCY $34

OTHER $20

TOTAL ON LOAN: $843 BILLION
AVERAGE FEE: 15BPS

EQUITIES



COMMON SHARES $787

ETF/ETN $30

DEPOSITORY RECEIPTS $23

OTHER $5

TOTAL ON LOAN: $845 BILLION
AVERAGE FEE: 68BPS

AVERAGE COMBINED ON-LOAN VALUE: $1.69 TRILLION

HOTTEST SECTORS GLOBALLY (EQUITIES)

ENERGY	HEALTHCARE	IT	MATERIALS	INDUSTRIALS
Fee: 121bps	Fee: 88bps	Fee: 86bps	Fee: 64bps	Fee: 60bps
$73 BILLION ON LOAN	$87 BILLION ON LOAN	$123 BILLION ON LOAN	$48 BILLION ON LOAN	$111 BILLION ON LOAN
HOTTEST INDUSTRY:	HOTTEST INDUSTRY:	HOTTEST INDUSTRY:	HOTTEST INDUSTRY:	HOTTEST INDUSTRY:
OIL & GAS DRILLING	BIOTECH	SEMI-CONDUCTORS	METALS & MINING	CAPITAL GOODS
Fee: 330bps	Fee: 164bps	Fee: 118bps	Fee: 97bps	Fee: 66bps
$7 BILLION ON LOAN	$26 BILLION ON LOAN	$25 BILLION ON LOAN	$21 BILLION ON LOAN	$80 BILLION ON LOAN

MOST PROFITABLE SECURITIES BY REGION MILLIONS, USD EQUIV.

NORTH AMERICA	EUROPE	ASIA
GAMESTOP $101	TRANSOCEAN $166	HANERGY $137
MANNKIND $99	GEMALTO $28	CELLTRION $82
CHESAPEAKE ENERGY $69	TALKTALK TELECOM $19	EVERGRANDE $33
FITBIT CLASS A $46	FINGERPRINT CARDS $14	HUISHAN DAIRY $30
MYRIAD GENETICS $46	AIR FRANCE-KLM $13	DAUM KAKAO $26

HOTTEST SECURITIES BY AVERAGE FEE

BPS	SECURITY	UTIL.
5810	EXONE	96%
5304	SHAKE SHACK	89%
4134	GOODRICH PETROLEUM	78%
3817	MANNKIND	96%
3815	AMIRA NATURE FOODS	98%
3814	VITAL THERAPIES	83%
3665	UNITED DEVELOPMENT IV	93%
3661	KANDI TECHNOLOGIES	96%
3598	ENERGY XXI	97%
3322	NOVACURE	82%

Making assets of assets

State of Illinois securities lending head Robert Crossen discusses how a volatile fiscal environment is affecting his securities lending programme

How important is securities lending to Illinois in terms of income?

There are some fiscal problems within Illinois at the moment as the governor and the state legislature have failed to agree on a budget for the 2016 fiscal year, which began on 1 July 2015. While unfortunate, it's the longest this state has ever gone without a budget.

This has impaired our ability to continue our programme of asset liability management because of the uncertainty regarding revenues and the timing of expenditures. There is still no official budget seven months on and all forms of state spending have been significantly reduced.

The portfolio of securities holdings now to has a much greater amount of cash back than was previously necessary to cover large dollar outflows and reduced revenue inflows. The lower level of our portfolio holdings has had an adverse impact on securities lending incremental income, but it still makes a solid contribution to our overall portfolio return.

At the same time, the state overall has lost additional revenue received from a temporary personal income tax and corporate tax increase that was enacted by law in January 2011 and expired in December 2015.

It's estimated that state revenue fell by $2.2 billion for the second half of fiscal year 2015. A rough estimated decline in revenue for fiscal year 2016 is $4 billion after the tax expired. Without the passage of a normal budget for fiscal year 2016, our conservative approach to keeping overall maturities short has had an adverse impact on our asset management and liability programme.

On the positive side, our net investment return from securities lending has climbed from the high 20 basis points (bps) to the mid-30 bps to 40 bps range, and in a low interest rate environment, our securities lending income has had a positive impact on our portfolio return.

What is your strategy under these conditions?

Our investments are typically in US treasury bills and we do buy a fair amount of US government agency coupon securities. Our strategy for short-term maturities is aided by conversations with our agent lender who indicated US treasury bills would do well in securities lending. We have done very well following this strategy. Our agent lender has indicated that this will likely continue. Our average net spread on loaned US treasury bills is 30 bps and that is very good.

For our asset liability matching programme, we look forward 12 months at a time and use US treasuries to match liabilities in monetary outflows from the state treasury—this translates into roughly $24 billion for a fiscal year or $2 billion per month on average. While somewhat constrained now, cash flows have been adequate to meet payment obligations.

We invest in US treasury bills to avoid carrying the cash forward through repo. Even with the Federal Reserve's interest rates so low and treasuries coming in at a low rate, our net take has remained at 30 bps to 40 bps since the programme began.

More recently, we have had to shorten portfolio weighted-average maturity in order to be more liquid, given our unusual fiscal problems, so we are taking a conservative approach of fewer than 90 days.

In terms of indemnification, we are covered on both sides of securities lending transactions. Our agent lender offers full indemnification on the loan side and also on the cash reinvestment side—that reinvestment is in short-term repo agreements.

Our utilisation rate has held at around 80 percent throughout the past year, although it did drop a little towards the end of the 2015 calendar year.

Do you require full indemnification of your securities lending transactions?

When we posted our request for proposal (RFP), we didn't contemplate the concept of indemnification from an RFP responder. One of our RFP responders did offer it and at the time we determined it to be viewed as 'value added'. Reporting and services offered by the responders were equally as important in our review of the responses received. We vetted the responder's abilities in these areas very critically to ensure that our office received the best package available.

What's being done about the state's budget?

State treasurer Michael Frerichs does have some influence as one of the five constitutional officers. Treasurer Frerichs is a former state senator and is keenly aware of the workings of the state budget as well as the detrimental effects of no budget. He has a very clear understanding of the state's fiscal issues and the need for having a budget in place for transparency and the effective management of the state. He has communicated his knowledge and perspective to the parties involved. The actual decision to agree on a budget remains with the governor and the state legislature.

Did your office, as a public body, have any problems launching a securities lending programme?

This Office of the Illinois State Treasurer renewed its efforts to establish a securities lending programme in the summer of 2007 through a state-mandated RFP process. In January 2008, after attempting an unsuccessful experience many years ago, our office officially engaged in a new securities lending programme. In the mid 1990s, we had to deal with the backlash from the Orange County debacle. Reverse repo was used by that entity, as well as other non-standard and high-risk investment vehicles, to engage in many unsound investment practices. What was meant to be a form of a money market fund for local governments eventually became a very precarious situation and that escalated to the point where it bankrupted the county.

The law for securities lending was actually passed prior to the Orange County situation. The law permitted the state treasurer to engage in securities lending. However, Orange County followed soon thereafter. As a result, there was an aversion to be seen to be doing anything like reverse repo, which unfortunately included securities lending. Over the passage of time, a greater and more positive understanding of securities lending prevailed.

Reverse repo is very different from securities lending, but the misunderstanding persisted and our conservative strategy just was not a good fit at the time we attempted securities lending several years ago. We discontinued a programme that was in place in the early 2000s.

When we started our current programme, we were on cusp of one of the greatest financial crises of recent memory, but we didn't actually have any problems and didn't lose any money because we weren't in any collateral pools. My understanding is that losses were incurred in some programmes involving collateral pool for certain entities.

Since inception it's been very successful and our agent lender is very good at providing us with an excellent service. This is especially true for the reporting requirements because, as a public body, transparency, following investment policy and state laws are all of primary importance.

There are lot more regulations in the pipeline in the US. Is there any specific one that you find is having a significant impact?

Overall, it hasn't affected our securities lending business. The increased regulatory emphasis on high-quality liquid assets has pushed some counterparties we do business with directly to withdraw from providing normal investing in overnight repo trades for our regular investment activity. This is not related to our securities lending programme.

> ***Since inception our securities lending programme has been very successful and our agent lender is very good at providing us with an excellent service***
>
> **Robert Crossen,** Head of securities lending, Illinois State Treasurer

Do you expect your strategy will have to change as a result of any of the regulations?

The changes in the repo market have not affected our securities lending programme, nor has the cost of indemnification, but what the future holds in either of these areas, I don't know. We will remain vigilant and nimble to navigate through the future.

On the other hand, the Dodd-Frank Act affects us downstream from a regulatory point of view and it's an ongoing concern for us because the full effect of it is gradually having an impact on financial markets in the US. Overall, our lending programme continues to run very well.

Do CCPs hold any interest for you as risk mitigation tool?

The use of central counterparties (CCPs) would be more of an issue for our agent lender than us specifically. It's another area in which we have discussions with our agent lender. We will always be open to new avenues of business and more effective ways to conduct our business while we maintain adherence to our investment policy and state law. **SLT**

The big FIS-h

With everything the new FIS has to offer, there is a huge opportunity for current and prospective SunGard clients, according to Tim Smith

How does SunGard and Astec Analytics fit into FIS? Is there any overlap in its existing business structure?

In fact, there is very little overlap in the two original businesses and there is much complementary technology. Though there is likely to be some reorganisation of certain business units, the majority of legacy SunGard businesses will be grouped together and be led by Marianne Brown.

How has the acquisition been taken from the SunGard point of view?

Given the context that it was a purchase by FIS, it has been viewed as an excellent opportunity for both sides of the business including retail and payments and wholesale and institutional. Now that the deal officially closed on 30 November, we are getting on with the job in hand.

How does the acquisition affect your budget and plans for the year?

We are focused on creating budgets and deploying resources in the most effective manner possible. Our team has been working with executive management and our marketing team to develop appropriate investment targets. FIS has a stated goal of reinvestment of 5 to 6 percent. We certainly hope to maintain or grow that investment where possible.

Is there any concern that you will now be expected to re-pitch your projects to new senior management figures, who may not have the same level of understanding of the products as you?

The majority of legacy SunGard divisions have been put in under the leadership of Marianne Brown. Marianne joined SunGard in 2014 and has been instrumental in the growth and management of the business. She will continue in this role now as part of the FIS executive leadership team.

What new innovations can the industry expect from you in the coming year?

We held a number of client forums around the world in Q4 2015 to test our ideas for innovative solutions against those who would be using them. From these meetings we received several good leads on areas that could be developed.

The introduction of intra-day reporting in the North American market in 2011 to 2012 was a major change in the market. Expanding to the global market means that it's an area ripe for development for our data analytics solutions.

We will be looking to expand our North American intra-day data service to the global market as well as provide more analytics of that data across the board.

There will also be a big push in the development of our reporting services, which traditionally serviced the beneficial owner space. We are now building a much wider spectrum of reporting across the whole securities financing industry.

As well as the new solutions being launched, we will also be working on new ways for our clients to slice and dice the data they receive and the ways it's delivered.

How is SunGard looking to prove its value to FIS?

Within the immediate Astec Analytics business, we have been able to present Gary Norcross, president and CEO of FIS, with a detailed analysis of short selling trends within FIS stock. As this information can be important to senior management regarding share price and investor sentiment, we were fortunate to bring this kind of immediate value to FIS and have the data available to prove it.

SunGard is usually the acquirer of companies, not the acquired. Does it feel strange to go by a different branding?

The combination of SunGard and FIS under the single brand of FIS is a huge opportunity for the company and our various solution

> ***We will be looking to expand our North American intra-day data service to the global market***
>
> **Tim Smith,** Senior vice president, Astec Analytics, FIS

sets. Though we are no longer SunGard, the new brand will only strengthen, over time, our commitment to the entire financial technology space.

Given the size of FIS, are there many opportunities for new synergies between other businesses within the group?

With everything the new FIS has to offer, there is a huge opportunity.

We have only been fully merged for a month and there are already opportunities presenting themselves. For example, we're discussing the potential of working with Capco on the need for consultancy on securities finance. We can now be brought into that discussion.

There may also be cross-selling capabilities with the banks and broker-dealers.

As a division within FIS, we will be open to many more points of contact between different service providers, which will mean we can offer value to other existing FIS divisions, as much as they can to us.

Further, we will be able to offer much greater value to our existing clients through these new connections at a time when the whole financial industry is moving away from silo-style services and toward a more open, connected way of doing business. **SLT**

Safe and liquid

Russia is making strides in repo, collateral management and securities lending. Maria Langouche of the country's National Settlement Depository explains

Collateral management is fairly new to the Russian market. Why is this coming about now?

Collateral management first appeared on the market about two years ago, but we were thinking about it for some time before that. Repo already existed in Russia, and it has been very successful. The difference is that, internationally, bond repo is an over-the-counter (OTC) product, and in Russia it is an exchange market. Like on many markets, our main liquidity provider is the central bank, so our main repo transactions come from repo or bilateral repo with the central bank, through the exchange.

Two years ago, the National Settlement Depository (NSD) and the central bank introduced OTC repo, which was something of a revolution. The central bank is still the main source of liquidity, but there is a collateral basket, and after the global financial crisis, liquidity has become quite precious.

We have proposed not only overnight repo, but repo for three days, for seven days, even for months. The central bank is even thinking about repo for a year, which means promoting the term and finding a way to secure good collateral. We have looked at what international central securities depositories (ICSDs) such as Clearstream and Euroclear are doing and the equities they propose as standard, and we're adapting some of those products to suit our own system. We have ended up with a lot of the same features—we have market-to-market and automatic selection of securities and replacements.

The main point to consider is that there was a need for this service in the Russian market. We started with about 100 clients and now, after just two years, we have more than 200 clients, including banks, brokers and investment companies. Of the total volume of repo in the market, we already represent 32 percent.

What we have had to do, and what we are still doing, is create a bank of information and teach market participants the benefits of collateral management. They have to adapt their systems and put in quite a lot of additional effort, so it's important that they understand the possibilities offered. The central bank has been very helpful in this, as it understands the international markets and the benefits of this kind of repo.

What do the new repo products mean for Russia?

We are certain that the facility will make the market more liquid and a lot safer. This is a difficult time in Russia—and everywhere—and when it comes to times of market stress, banks can find themselves in some difficulty. If money can be taken out of the banks in a way that is safe for the whole market, that will benefit everyone.

We hope that our efforts will also make the market more interesting, and we see this creation of a repo market as a first step, and a service that we intend to expand. We are planning to propose the same kind of repo with the central bank, offering collateral management to on-exchange transactions, too. This will use the connectivity of the shareholders, including the Moscow Exchange, and allow us to include more and more participants in to the process.

In the future, we are also thinking about introducing securities lending. Repo in Russia has two purposes, to avoid failing to deliver securities and to facilitate borrowing. Securities lending is only used for avoiding failing to deliver securities, so why not introduce a specific mechanism based on repo to help make the market even more liquid and even safer? We are working on that initiative, but it might not come to light until 2016 or 2017. It will involve changing legislation and adapting our systems, and a lot of work with the market.

What are the benefits of developing a collateral management business from scratch?

We have learnt a lot from the experience. There is always a difficult choice: buying a system that already exists or developing it from scratch.

There are existing systems out there that allow securities lending and collateral management that could be extended to other products, because the technology is so perfect now that it can be easily applied to various platforms. We considered it carefully and decided that it would be more interesting for us to develop it ourselves.

Doing it this way adds an element of safety. Considering that we are still in the midst of a crisis, and there is still a question of possible sanctions, we have to remember that this service is a crucial element of the Russian infrastructure. It's like the circulation of blood—the liquidity that comes from the central bank is circulated around the other participants, and if it stopped there could be a crisis. We have to take responsibility for this.

On top of this, it might not be perfect just yet, but in the near future we expect to be able to offer our own solution to other countries, such as our colleagues in the Commonwealth of Independent States, who could learn from our experience.

We are happy that we chose to do it ourselves, but we are open to alliances. We have been in discussions with Clearstream and Euroclear about possible collaborations in the future, joining the ICSDs to create a link between our systems that could allow, for example, Russian participants to use euro bonds in the international environment, for collateralising Russian transactions, and vice versa.

Is it important for Russia to fall in line with international standards for collateral management?

It is very important. Even with the political pressure on Russia, we must continue our work on the infrastructure side, and we want to make sure that everything we do corresponds to international standards. For example, if we start from the basics, in the financial industry everyone is using the ISO 15022 format applied for SWIFT communications, and this will soon upgrade to ISO 20022—our collateral management project uses the same format, keeping up with international standards.

Secondly, we are using international documentation for repo transactions, which correspond to the International Capital Markets Association requirements.

We are looking at what international regulatory organisations are proposing and what is being adopted by internationally, and we are also trying to have an open infrastructure that will allow us to be as technologically connected as possible. **SLT**

In the future, we are also thinking about introducing securities lending. We are working on that initiative, but it might not come to light until 2016 or 2017

Maria Langouche, Vice president,
National Settlement Depository

Securities financing technology trends to watch

Blockchain, big data, industry utilities and modular solutions are all expected to play a part in securities financing, says Jerry Friedhoff of Broadridge

About 40 years ago, a small group of pioneers launched the modern securities lending industry in the UK and US. These pioneers developed the basic processes and services necessary to make these functions a fundamental part of today's global capital market operations. Incremental changes to the practices and technologies deployed by these financing desks and their supporting operations have been made over the years, but more recently there have been tectonic shifts in how these business lines operate.

The regulatory and market changes that have already been rolled out, or will be deployed in the near future, will touch every firm involved in securities financing. It's hard to predict at what point regulations and market structures will begin to wane but instead of bemoaning the changes, perceptive and agile firms are devising plans how to take advantage of them. New business models, evolving trade structures and advanced collateral optimisation strategies will help progressive market participants find ways to make money in tomorrow's securities financing landscape. Technology will be one enabler to allow such firms to adapt and thrive.

Within the securities finance space, there are four developing technology trends that bear watching over the next several years. These trends may trigger some near-term changes in traditional practices, but they will also create long-term competitive advantage for firms agile enough to take advantage of them.

Blockchain

In recent months, financial institutions have become increasingly interested in the blockchain distributed ledger technology. Numerous firms are jumping into this area and beginning to trial blockchain applications across various back- and middle-office 'use cases'. The potential of this new technology is huge, but so are the challenges. The idea of providing more efficient, secure and transparent transactions using digital currency seems like a possible panacea for many of the operational challenges capital market firms have faced for years.

The securities lending sector has been identified as one of the areas where this distributed ledger could link beneficial owners directly with end users, reducing costs and timing delays. Initially this sounds great, but the implications to firms' operational workflows, proprietary trading strategies and desire for anonymity will need to be carefully thought out. In the securities financing space, participants have traditionally wanted intermediaries involved for indemnification and anonymity reasons. In addition, the lack of a regulatory framework or industry-wide acceptance for blockchain systems could cause compliance and legal headaches for capital market firms. Regardless, the financial services industry is taking note of blockchain technology as evidenced by the number of startups looking to make a splash in this area.

Big data

Big data is another key technology area being discussed in boardrooms across the financial services sector. This next generation evolution of data warehousing, business intelligence and data management is intended to give firms unprecedented insight into their own operations, client data (for example, counterparty risk) and markets. However, harnessing the power of big data does not lie in the installation of the technology itself—but applying smart approaches to coax out actionable insights from the massive amount of data collected. In the securities financing sector, some firms are trying to leverage big data solutions to track trading activity, news reports and internal asset availability. The jury is still out on how effective these powerful tools are in actually driving improved margins, but the potential for competitive differentiation exists.

Industry utilities

Securities financing desks have been facing a prolonged period of regulatory and market challenges that are profoundly affecting their profitability and place within financial institutions. Demands for reduced counterparty risk amid a sustained period of low interest rates have forced firms to look for third-party intermediaries to help mitigate transaction risk and provide cross-border infrastructure services whose cost can be mutualised across industry participants. A number of industry utilities have expanded or started over the past five years to provide independent shared solutions to assist in the movement of collateral in a way that meets evolving regulatory requirements.

These firms have the resources and expertise to help securities financing businesses with fixed cost solutions that meet internal and external control and data security requirements. It's expected that these industry utilities will continue to expand their offerings in the coming years to meet the needs of the global repo, securities lending and adjacent collateral management markets.

> ***Industry utilities will continue to expand to meet the needs of global repo, securities lending and collateral management***
>
> **Jerry Friedhoff,** Managing director of securities finance and collateral management, Broadridge

Modular solutions

The last trend is one that has been growing for several years, but with less fanfare than the other three. More and more or our clients are looking for point solutions rather than monolithic applications that handle a wide array of activities. Even though end-to-end, all-inclusive solutions allow procurement managers to tick off many boxes on their competitive analysis, the securities financing desks usually end up using only a fraction of the application's capabilities. By modularising securities financing solutions into distinct components that can be installed, upgraded and also de-commissioned without requiring major IT engagements, repo and securities lending desks can gain business value faster and more economically.

At Broadridge, we are actively involved in all four of these emerging trends to ensure we meet the needs of our diverse global client base. It is an exciting time to support the trading, IT and operations teams tasked with evolving their firm's securities financing capabilities quickly and economically. Now more than ever, it is essential that move to where securities finance is going to be, and not where it has been. **SLT**

Business as beneficial

With interest rates finally rising in the US, experts discuss what the future has in store for beneficial owners and their agent lenders

James Slater
Executive vice president and global head of securities finance
BNY Mellon

George Trapp
Head of North American securities lending client service
Northern Trust

Paul Lynch
Chief operating officer
eSecLending

Chris Benedict
Director
DataLend

Tim Smollen
Global head of agency lending
Deutsche Bank

Paul Wilson
Global head of agent lending product and portfolio advisory
J.P. Morgan

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

Michael Saunders
Head of trading and investments, North America
BNP Paribas

Owen Nichols
Managing director
State Street Global Markets

How is the US market faring, particularly after the rise in interest rates?

Chris Benedict: Demand to borrow US securities remained strong in 2015, even after the Federal Reserve raised interest rates by 25 basis points (bps) on 16 December 2015.

There was an average of $954 billion worth of US assets on loan and an average of $7.44 trillion in lendable assets for the US in 2015. The US market averaged fees of 39 bps with an overall utilisation of 12.8 percent for the year. Securities lending revenues for the US grew 21 percent from approximately $3.11 billion in 2014 to about $3.78 in 2015. The US market remained a predominantly general collateral market punctuated with specials in 2015, much as it was in 2014 and 2013.

George Trapp: Since 2016 began, the US market has been reacting to global concerns. There has been an increase in volatility across the global markets. Nominal interest rates still remain at historical lows despite the modest 25 bps increase in the federal funds target range, however, that move was well anticipated and has had little impact on the broader financial markets.

From the securities lending perspective, increased volatility has meant large swings in mark-to-market activity and continued, steady demand in the US market across all asset classes. Short-term rates have settled into their new range and been relatively steady as anticipated. As part of a larger trend, there is less reliance on cash collateral and US beneficial owners are seeing a larger portion of non-cash collateral being pledged by borrowers.

Paul Lynch: The US economic market shows positive signs of moderate growth and stability. The US equity market has experienced volatility due to the price of commodities, global market influences (China), high yield and emerging market credit issues, and the forecasted rising cost of capital. Interest rates are rising, which means the cost of cash is increasing.

There is usually a strong correlation between increased borrowing costs and equity valuation volatility, especially for companies that have levered or have stressed operating profit business models. These are factors that will contribute to a growing securities lending market in 2016. Hedge fund and short activity should continue to grow into 2016 across individual names and sectors as fundamental long and short analysis incorporates the rising cost of cash.

Tim Smollen: In terms of managing interest rate risk, we are very well positioned because we are not relying on the duration of our cash collateral investments to boost revenue. Our model is not intended to capture wider spreads by mismatching assets and liabilities.

Instead, we are focused on getting the rebate rate (fees) right, and maintaining spreads as rates track upwards. Our strategy to refrain from adjusting rebate rates in lock step with the Fed has worked very well for our clients as we avoided spread compression. In fact we increased spreads as the asset side re-priced almost immediately.

Paul Wilson: The US market fared fairly well throughout 2015 and was especially strong in the latter part of the year. Specials activity in US treasuries picked up sharply in Q4 following stronger than expected employment data. The five-year issues, followed by the three- and two-year issues, were the strongest in demand with a trend towards specials in treasury bills over quarter ends.

There was increased usage of the Fed's overnight repurchase programme, which statistics show rose from $58 billion to $138 billion on 30 November, and highlights a product shortage in the market. In equities, the energy, healthcare, technology and consumer sectors were the most in demand with earnings further boosted by corporate activity led by the GE/Synchrony Financial exchange offer.

We note that the borrowers are increasingly preferring non-cash collateral. With the Fed rate rise taking place as anticipated in December, cash collateral investment activity reflected shorter term investments and mixed with floating rate investments to provide a level of protection against rising overnight rates. While it has been some time since we have been in a rising rate environment, it is something we have been through previously. Our securities lending investment team has been navigating this scenario for most of 2015 in anticipation of the US interest rate rise, but this cycle has been more challenging as high quality issuers are scarcer at the short end of the rate curve.

Michael Saunders: The market responded quickly to the December announcement, as money market yields moved upward reflecting higher benchmarks. General collateral rates took several days to normalise, while top-tier issues as well as trading outside of the general collateral bucket remained steady for the most part.

We believe the likelihood of further rate increases makes this a good time for clients with appropriate reinvestment strategies and risk profiles to consider lending approaches such as overnight/term or interest-rate mismatch portfolio strategies. Going forward, we could see more beneficial owners returning to the US lending space—there has already been an increase in dialogue among some clients, and so we continue to offer solutions to monetise potential opportunities in the making.

Scot Warren: From the central counterparty (CCP) perspective that OCC brings to the marketplace, we see continued growth in our stock loan programme. Month-to-month activity grew throughout 2015, with overall activity up 16 percent from 2014 with nearly 1.4 million new loan transactions in 2015. Average daily open loans were up 12 percent. As OCC continues to see interest from the industry and plans to expand in this area in 2016, we brought on new members to build up our stock loan programme last year.

Owen Nichols: The US securities lending market has been doing very well and demand for US equities in particular has been favourable. Two of the main themes we are seeing now are increasingly strong demand for US equity specials, and widening spreads for US short rates.

With respect to US equity specials, demand for deep specials continues to be robust—Q4 2015 will be one of the strongest on record. In 2015 overall, US equity lending returns in total were the strongest we've seen in five years, outpacing 2012's outstanding performance when demand for a number of social media initial public offerings, alternative energy, and for-profit education positions produced record returns. For 2015, the drop in the price of crude oil has brought a number of energy names to the top of most managers' short position list. Demand for biotech stocks also contributed to these rich returns.

With respect to US short rates, after seven years of a -0.25 percent Fed target rate, cash reinvestment desks have welcomed the Fed's December action. Markets have responded to the tightening and anticipated follow-through with a widening of spreads between overnight funding cost indexes and 90-day cash investment indices. These movements should improve reinvestment spreads and create trade opportunities.

How is demand for US beneficial owners' securities?

Lynch: Overall demand has been good year-over-year. High spread borrows, known as special borrows for a limited amount of securities, continue to generate a healthy percentage of beneficial owner revenue. Moderate spread borrows, known as warm borrows, had been growing in 2015 and we expect them to accelerate growth throughout 2016. Low spread borrows, known as general collateral borrows, began growing in 2015 as prime brokerage long supply decreased, broker-to-broker activity decreased, and some lending agents cut back on general collateral lending due to regulatory costs. We expect the demand for positive low spread business to grow throughout 2016.

It should be noted that collateral and term structure will play important roles in securities lending demand in 2016. Non-cash collateral and term structure will be important factors for structuring trades with optimal risk-adjusted performance for the beneficial owner and optimal regulatory capital costs for the borrower.

James Slater: Demand for borrowing securities continues to evolve in the new landscape. There are many factors that are affecting demand, but the main factors are regulation and its goal to reduce risk and increase transparency, which are causing structural changes to the marketplace.

To better understand the demand for borrowing securities, it's best to analyse demand by product or asset type. Fundamental demand for borrowing equities continues to be strong, however, accommodative monetary policies have had an impact on the general direction of the financial markets. As a result, some investment strategies would have been challenged as evidenced by their performance in 2015, although in early 2016 the equity market direction has turned, which may provide some hedging/directional-related demand.

Other investment strategies, such as event-driven, could be well positioned as 2015 had the highest mergers and acquisitions activity in the US since 2007. The momentum for event-driven strategies in 2016 seems to remain, but time will tell if this momentum materialises into securities lending opportunities.

Another area that provided some opportunity for demand growth was liquid alternatives. Despite a leveling off from the frothiness in 2014 and early 2015, it will provide some demand for securities finance and borrowing securities.

For fixed income demand, there are a few key influencing factors. Balance sheet efficiency is presenting opportunities for beneficial owners that provide collateral and term flexibility. Regulatory demands around balance sheet ratios and increased collateral demands for central clearing have increased borrowers' need for high quality liquid assets (HQLAs). This demand is expected to continue. Some would point to the notion that collateral might be viewed as the new cash.

In addition, the recent movement in US interest rates has provided some scarcity value in select treasury securities, and the general flight to HQLA in response to geopolitical circumstances continues to fuel demand. New margin rules for non-cleared derivatives activity and looming money market reform is anticipated to result in further increased demand for government securities/HQLAs.

While the Fed, through its reverse repo facility provides access to HQLAs for some borrowers, it remains to be seen whether it satisfies the demand created by the ever increasing need for HQLAs. Offsetting some of the growing sources of demand for HQLAs is that there is less intermediation on the part of dealers to hold and support this activity due to its capital intensity and relatively low profit margins.

Benedict: Energy, IT and healthcare sectors were all in focus in 2015. Energy commanded average fees of approximately 155 bps in 2015, well above other sectors this year, mostly due to the selloff in oil. The oil and gas drilling and coal and consumable fuels industries were especially hot within the energy sector, with average fees to borrow coming in at 339 bps and 213 bps for the year, respectively. Utilisation for these industries was also higher than average at 49 percent for the drillers and 44 percent for coal and consumable fuels.

IT was the second-hottest sector globally with average fees to borrow at 87 bps and 11 percent utilisation for the year. The healthcare sector was just behind IT in terms of its borrowing fees for 2015, coming in just 1 bps shy at 86 bps with an average 8.5 percent utilisation.

Smollen: We think demand is good, but that depends somewhat on one's business model and the client's holdings. Deutsche Bank markets selectively to beneficial owners with attractive, diversified portfolios. Keep in mind that even desirable mandates include securities with low demand characteristics, so we see our role as determining the liquidity and rebate rate for every holding.

Our clients tend to be long-time lenders with defined expectations as to what a 'right-sized' programme should be. That means not lending securities where the risk-adjusted returns would fall short of client expectations. We call it optimising within a risk-constrained set of objectives. More than that, it is a sustainable business model.

Wilson: From a supply perspective across US beneficial owners, this has been one of our strongest years, coupled with an even greater level of engagement and participation by beneficial owners. Existing clients have been quite open minded towards expanding, reviewing cash reinvestment guidelines (and options given money market reform), diversifying collateral, reviewing restrictions/parameters and being more active about complex markets, such as Taiwan and Malaysia.

We have seen new beneficial owners clients come to market and others re-entering the market since the global financial crisis. Our third-party business has grown substantially as beneficial owners become increasingly focused on matching their risk/reward profile to an agent. Without doubt, indemnification remains the number one topic of discussion across beneficial owners. The increased focus and debate about indemnification has undoubtedly led to a better appreciation of the relative quality and differences of agents in the indemnification offerings.

Trapp: Demand continues to be strong for US beneficial owner's securities, however, the market has moved to more of a specials market with general collateral making up a smaller portion of earnings, especially for portfolios concentrated in US government fixed income securities. It is anticipated that diversified portfolios will continue to be in demand because they will likely include specials across a variety of markets.

Saunders: While new regulatory mandates have weighed on liquidity to some extent, we are still seeing consistent borrower demand for all of our clients' asset classes, particularly around issues that trade special such as Amercian depository receipts, common equities, corporates and US treasuries. Intrinsic lending continues to be the strategy of choice for domestic owners, and we believe that bodes well for such programmes in the year ahead.

The ongoing sell-off in commodities has been keenly felt within the high yield and emerging markets, compelling borrowers to secure supplies linked to these segments as well as commodity sensitive firms. Meanwhile, the imposition of more stringent capital-adequacy/liquidity coverage requirements under Basel III and the US Dodd-Frank Act has raised the appeal of HQLAs, compelling HQLA owners to consider capitalising on the increased demand among large institutional borrowers.

How are they and their agent lenders innovating to boost returns while keeping risk to a minimum?

Wilson: While we see increased beneficial owner engagement and a willingness to review parameters, we have not seen significant changes in programmes and programme structures. Risk management, indemnification and operational efficiency rightly remain the cornerstones of lending programmes for US beneficial owners. Any changes that may boost returns need to be evaluated against those parameters.

Macro issues affecting the industry on borrowers and agents include regulatory change and the pace it is implemented by jurisdictions. This may create challenges for program development for some beneficial owners. We continue to liaise with beneficial owners on alternative (non-traditional) structures and transaction types, which could create some additional value to beneficial owners.

Trapp: The metrics, analytics, and trading tools being used to price demand and distribute inventory are the most significant innovations over the past several years. New markets continue to offer opportunities for innovation and increased income for beneficial owners. However, we have observed that innovations in trading have led to the largest gains in and revenue for beneficial owners.

Collateral diversification is also an important aspect to maintaining and increasing returns for lenders. The trend to non-cash collateral continues and those lenders willing to accept a broader range of collateral are likely to be well-positioned to maximise revenue within their acceptable risk parameters.

Lynch: Innovation is occurring on multiple fronts. Flexibility regarding forms of collateral has been a high growth area. Various forms of non-cash collateral from US and non-US counterparties that have appropriate haircuts that are marked-to-market daily, have a daily value-at-risk (VaR) calculation, and are appropriately stressed for VaR and liquidity needs are contributing to risk-adjusted returns.

Matching the method of distribution with borrower demand is also contributing to risk adjusted returns both from a technological perspective and a structural perspective. We see increased demand for structured exclusives versus discretionary lending in certain markets and certain asset classes. Auctionable exclusives for 2016 have had significant growth in demand and performance.

Nichols: We continue to evaluate new equity lending markets and collateral types to add incremental return for lenders while managing the various risks associated with each trade type. In regards to collateral reinvestment, agent lenders are working closely with beneficial owners to adapt reinvestment guidelines to reflect a new reality in which credit ratings are less relevant within the industry and increasingly liquidity is found from non-traditional sources. We've also been working to develop innovative approaches to utilise agency lending as a source of leverage and liquidity for our client base.

Smollen: We innovate through collaboration with our clients given that any solution we develop has to comport with client risk tolerances and return expectations. We are a third-party agent, so our clients expect us to be in regular contact and proactive in dealing with change and offering up ideas, solutions and options. This involves continuously evaluating programs and client initiatives to boost returns that might involve areas such as enhanced trading structures, non-traditional counterparties, non-traditional collateral and cash reinvestment solutions. The thing about our programme is that it never sits still—we are constantly evolving.

In terms of how we manage risk, we employ an enterprise-wide approach to risk management that entails oversight and consultative input from

numerous independent risk units. We have teams, for example, that advise on market reforms and regulatory risk across both agent lending and principal borrowing activities of Deutsche Bank.

This positions us extremely well to advise clients on the stress factors affecting both agents and borrowers, and possible solutions, such as incorporating non-traditional counterparties into a clients' strategy, while still retaining the ability to indemnify certain risks. Additionally, we measure balance sheet and indemnification cost and use this to help guide the business when contemplating trade opportunities, such as lending in one jurisdiction and accepting collateral elsewhere.

Saunders: Innovation and customisation continue to fuel our securities lending practice. Portfolio maximisation, for instance, allows us to create customised lending and reinvestment solutions on a client-by client basis, whether it be intrinsic only or conservative overnight reinvestment options using repo/money market mutual funds, or more sophisticated programmes that centre on term lending or similar structures. We also prioritise operational efficiency and risk-mitigation strategies, which we believe are just as important to clients as enhanced returns, perhaps even more so in some instances.

Additionally, we strive to be at the forefront of new global opportunities—our business currently extends to 48 different markets, with solutions that encompass emerging as well as other international strategies. Our team of network experts helps us stay informed about lending in new markets and regulatory initiatives in the making. They also help us in implementing funding structures that can benefit owners and borrowers alike. Closer to home, we continue to monitor discussions aimed at amending Securities and Exchange Commission (SEC) Rule 15c3-3, with an eye toward utilising equities as collateral should such changes occur.

Benedict: Agent lenders are using more benchmark performance reporting tools to ensure an optimal return for their beneficial owner clients. For many beneficial owners, securities lending is an integral part of their investment strategy as lending revenue can have a positive impact on their portfolio's overall return.

To optimise the return to their portfolios, and to better understand market trends and opportunities, both agent lenders and beneficial owners are engaging directly with tools like DataLend's Client Performance Reporting suite. This allows them to achieve a true 'like-to-like' view of their performance benchmarking tool, where they can select the most accurate peer group possible for their clients based on similar fiscal locations, legal structures, securities on loan and dividend rates.

Slater: Risk management is a cornerstone to any securities lending programme. With that in mind, there are several avenues for clients to derive returns from securities finance. These can range from the well-known intrinsically valued lending programme to the new collateral paradigm that is evolving, ie, the HQLA supply shortfall mentioned above. This can mean lending into the increasing demand for HQLAs, to capturing opportunities related to term financing, and/or engaging in collateral transformation trades. These strategies require establishing a rigorous and comprehensive risk management oversight programme. Counterparties, margin, market and trading activities must be carefully considered before engaging in a transaction followed by continuing oversight over the programme to ensure the goals of the programme remain in place. As the pace of change is ever increasing, it is important that there is active oversight and governance for these programmes.

Another area to keep a close eye on is money market reform. Depending on how money market mutual funds adapt, and should they follow the path of some early movers in transitioning from prime funds to government funds, one would expect a widening of spreads for corporate issuances as demand for government securities increases. This in turn will increase demand for lenders willing to extend term and provide flexibility around collateral.

Participants are continuing to push for mutual fund rule changes in a bid to optimise collateral usage—how would these changes affect the US business for either side of the trade?

Lynch: The industry has been advocating for changes in the form of alternative non-cash collateral, namely, equities as collateral. Alternative collateral will require mutual fund rule changes as well as broker-dealer SEC Rule 15c3-3 changes. There is a strong argument that an equity fund should be able to accept equities as collateral assuming that it is appropriately diversified, liquid, has a daily VaR, has periodic stress tests, and has a sufficient haircut. Equities as collateral could be beneficial to both sides of the trades if structured appropriately.

Also, some members of the fund industry are looking to more efficiently use their cash collateral as a treasurer function within the fund. As mutual funds become more efficient, the question is why pay for outside lines of credit for subscription/redemption activity and over-the-counter (OTC) collateral needs when a fund can create cash collateral from lending activity? Why not minimise expenses of the fund for shareholders? Innovation in this area continues to be explored with the need for rule interpretations.

Benedict: Should collateral guidelines for mutual funds be amended, the use of non-cash collateral will likely increase in the US market as regulatory requirements such as the leverage ratio and liquidity coverage ratio make pledging non-cash collateral more capital efficient for borrowers. Currently, non-cash collateral is pledged against only 36 percent of all securities lending transactions in the US, whereas that same collateral type accounts for a much higher percentage in the European, 80 percent, and 73 percent in Asian markets.

Smollen: We are of the mindset that we should explain to beneficial owners market place events, how it might affect them, and their options. We have worked with industry groups to do the same for the broader constituencies. As far as US mutual funds, the ultimate decision makers are the independent fund boards. We work consultatively with them and their advisors as they decide what is best for fund shareholders after their regulators approve any changes.

Nichols: Collateral optimisation will be a key driver of the securities finance business going forward in light of the regulatory challenges faced by both agent lenders and borrowers. Current discussions are on enhancing the ability of borrowers to optimise their collateral usage in a manner that is most efficient from a balance sheet perspective. Given the changes to leverage limits globally, and particularly for US global systemically important banks, the ability to enter into less punitive balance sheet trades, such as trades that can be netted or non-cash trades, will continue to be a priority for borrowers. These trades have limited direct benefit to the agent lenders, but similar to central counterparties (CCPs), they provide an opportunity to maintain demand and protect trade flow.

How are lenders adapting to regulatory change?

Wilson: US beneficial owners are engaged and thoughtful about understanding regulatory change, the impact on the industry and the impact on their lending programmes. On the whole, we have seen them adapting to regulatory changes by becoming more flexible in their approach to lending and their overall lending parameters. Regulations and rules such as the liquidity coverage ratio (LCR), supplementary leverage ratio (SLR) and net-stable funding ratio (NSFR) mean that borrowers are now looking to lock up loans for term, rather than on open. Additionally, the SLR and NSFR have also meant that borrowers

are more likely to post non-cash collateral, a big change in the US markets. Lenders have had to get comfortable with taking additional types of collateral for longer durations than they have in the past.

Lastly, the increased cost of capital means that clients are now re-assessing the breadth and depth of the indemnity and discussing this with their agent lenders. Since the crisis, lenders who continue to value lending as a revenue source have become more actively involved in their lending programmes, which is a positive step. The lenders that are interested in staying abreast of regulatory change should continue to receive value from lending.

Slater: While regulation continues to reshape the lending market, beneficial owners are making the changes necessary to take advantage of the opportunities created by new regulatory requirements. For example, liquidity ratios and mandated clearing have created new sources of demand.

This, coupled with the impact of increased leverage ratio requirements on borrowers, has resulted in a significant increase in the number of transactions collateralised by securities collateral. This makes collateral flexibility key to maintaining utilisation and taking advantage of these new opportunities.

Many lenders have already expanded or are in the process of expanding their collateral guidelines. Europe has always been more open to securities collateral in general, but now US lenders appear to be accepting of a wider variety of securities collateral including equities.

New regulations are also creating collateral and liquidity challenges for some beneficial owners. Traditional sources of liquidity have become limited and expensive at the same time that collateral requirements for beneficial owners are increasing. As a result, many beneficial owners may become interested in the role that securities lending can play in helping them meet their liquidity and collateral needs while seeking to reduce costs and improve fund returns.

Nichols: Regulatory change is a continuous process that is impacting both agent lenders and borrowers. The agent lenders are becoming increasingly focused on the amount of risk-weighted assets (RWAs) being consumed by indemnified transactions and the return on capital associated with such transactions. In the US, some banks are being constrained by the standardised approach for calculating RWAs based on the Collins Amendment and even those who are not constrained under this approach from a regulatory capital perspective are beginning to feel the effects due to the standardised approach being the only option for comprehensive capital analysis purposes. Additionally, agent lenders are awaiting the finalsation of the Basel large exposure/Dodd-Frank Act 165(e) rules.

These regulations as currently proposed would utilise the standardised approach and would likely require a reduction in lending to some of the largest borrowers. At the same time that the agent lenders are facing this regulatory landscape, the borrower community is either being impacted or will be impacted by the new leverage rules, RWA constraints, the NSFR and the LCR. As a result of these regulatory changes, the use of non-cash collateral and term trades have increased, certain asset classes have been re-priced, and the re-pricing of certain client relationships, or explicitly pricing indemnification, has occurred. Additionally, lenders are exploring other routes to market that have lower regulatory hurdles, such as central counterparties or utilising third party support in lieu of indemnifications. These efforts are ongoing and full implementation may be longer term in nature.

Trapp: Beneficial owners are experiencing the indirect impacts of regulation through the modified lending behaviour of other market participants, such as borrowers and agent lenders. This could in turn cause beneficial owners to make changes to their own lending programmes. For example, the demand for borrowers to pledge more non-cash collateral and utilise term lending has increased across the market. Similarly, beneficial owners are adopting expanded collateral guidelines in order to maintain levels of lending activity that are consistent with their historical trends.

Saunders: Using thought leadership tools such as webinars, newsletters and roundtables to keep clients apprised of specific regulatory rulings remains highly important as is a consistent direct line of communication on such topics. The key challenge is finding common ground so that all parties are able to benefit. We believe that maintaining this kind of dialogue between clients, industry groups and dealers is key to achieving a fully transparent lending programme. Accordingly, we anticipate and plan on holding further discussions throughout the year as the regulatory environment continues to evolve. The experts at BNP Paribas are keenly watching and participating in all relevant discussions on a global basis.

Smollen: Our clients are interested in understanding the impact of change on the business, including stresses on agents and counterparties. While many are constrained by policy or statute, others enjoy the flexibility to rethink long-standing ways of doing business. In some cases, the movement is small and measured, but we are seeing receptivity, which is essential. Ultimately, dealing with market reforms may yield rewards, including alternate sources of liquidity and new reinvestment opportunities in a less intermediated future. We think that we are well situated as change unfolds.

How are collective investment schemes such as ETFs changing securities lending? What about synthetic products such as single stock futures and swaps?

Trapp: Exchange-traded funds (ETFs) are a great example of a product that has benefitted from securities lending. Securities lending has brought liquidity and incremental returns to ETFs, which in turn have benefited the end users, investors, of the ETFs.

Lynch: ETFs provide two forms of lending: (i) the 'registered fund' that lends the underlying assets of the ETF, similar to a mutual fund; and (ii) the beneficial owner/investor in the ETF lending the ETF holding. Demand for lending the ETF holding has risen over the past few years. Specific index ETFs such as the Russell 2000, High Yield, Emerging Markets and Junk Bonds have traded at valuable spreads. Similarly, certain sector ETFs and country ETFs have also traded at great value. Demand for these securities is due to the ease of shorting an index, sector or country. Swaps continue to be a tradable alternative to owning a physical security and lending it. They add complexity with investment guidelines, investment disclosure, and tax consequences, but are a viable solution for lending in emerging markets or for any market. It is important that the beneficial owner understands the swap, understands all of the returns, flows and netted expenses, and makes a suitable investment decision versus owning the security and lending it.

Smollen: ETFs have exploded in popularity with investors, as well as with short sellers seeking exposure to markets or asset classes that can be difficult or impossible to short otherwise. This has driven record securities lending revenues on these products based on resilient demand. It is no surprise that many prime brokers have now created and staffed desks to exclusively trade this product. We've reacted to that and trade the ETF book separate from the US equity book.

Conversely, many counterparts have looked to use ETFs as collateral as more and more are being held within inventory for future sale. We are extremely careful in accepting ETFs as collateral as there have been well publicised tracking errors to the constituent parts in down markets, and many ETFs increase correlated risks within stressed markets. Our acceptance of ETFs is dynamic in that approvals are based on current market conditions.

Nichols: Obviously, ETFs have been loaned for some time and are used as a hedging tool as well as an access point to markets that may be difficult to enter. We have noted increased demand spreads over the last year as borrowers' balance sheet constraints have limited their ability to create ETF baskets within their business. Regarding single stock futures, they certainly do compete with our business but on a very limited number of positions. However, this trade is obviously attractive to prime brokers, as they are generally off-balance sheet transactions.

Saunders: During the past year, ETFs became more visible than ever before, and with good reason. ETFs can offer the potential for greater utilisation and liquidity within the marketplace, particularly portfolios tied to specific sectors or regions—for instance, metal, mining, energy and other commodity-based ETFs have been unusually strong of late.

Accordingly, we are seeing a greater number of ETF investors actively interested in securities lending due to the revenue generating opportunities within.

Appetite for vehicles such as swaps, derivatives or single stock futures is very client-specific, and, when applicable, BNP Paribas can offer appropriate services and solutions. For the most part, programme participants have remained focused on generating incremental income through basic lending transactions. However, we regularly provide guidance on all other opportunities within the marketplace.

This year could well be the year of the CCP—what are US beneficial owners saying about central clearing that they haven't before?

Warren: In 2015, OCC saw an increased interest in central clearing for stock loan, and a need for more education from the agent lenders on behalf of their beneficial owners in terms of what benefits they can derive from a CCP such as OCC. We believe market participants are no longer debating whether central clearing is beneficial for the stock loan industry. Instead, they are looking at how a CCP solution can in fact enhance securities lending activity for lenders as well as the broker-dealer borrowing community.

Slater: Central clearing models for the agency securities lending market are still nascent. BNY Mellon has been working with industry participants to develop a clearing model that meets the needs of beneficial owners. It is expected that a workable model will emerge in the near future. This year may be the year that we begin to see some initial transactions. However, certain regulatory changes will be needed to allow for most US beneficial owners to participate broadly.

The move to central clearing is being driven in large part from the pressure on dealers' balance sheets as a result of increased leverage ratio requirements. Central clearing will allow the dealers to maintain their existing volumes, but in a more balance sheet efficient manner due to increased netting benefits. As a result, CCPs will become an important distribution channel for our clients' assets that will allow them to maintain balances and in some cases, obtain better pricing.

It is expected that the decision to utilise central clearing will develop as a point of trade discussion just like any other loan term. The negotiation with respect to how the trade will be cleared (centrally or in the traditional bilateral manner) will likely be based upon the benefits that the borrower may derive from central clearing. Accordingly, it is expected that a pricing differential would develop between centrally cleared loans and traditional bilateral loans.

Trapp: The questions still remain from the beneficial owners about what benefits they will see and how the CCP model compares relative to a typical lending transaction.

Nichols: At this point in time both agent lenders and borrowers are working closely with a number of CCPs to develop viable options for agency securities lending transactions. A number of issues remain to be resolved before CCPs experience significant flows from agency securities lending business. Current offerings are limited in the markets available, and operational efficiencies, especially around corporate actions, must be developed before there is a wholesale adoption.

We are currently working with CCPs to ensure that these issues are resolved in such a manner as to protect the interests of the beneficial owners that we service. As such, conversations with clients remain in the infancy stage with the ability to add or protect trade flow being the primary discussion point.

Lynch: US beneficial owners are watching and educating themselves as the CCP model evolves. The securities lending CCP model has evolved faster in Europe but current regulatory registrations do not allow US beneficial owners to participate. A US CCP model is still in the concept stage. I believe most beneficial owners are curious and are willing to review models as they come to market, but are waiting to see what they are and what value it brings to them.

Benedict: As CCPs offer both borrowers and lenders a more capital-efficient route to market, there has been increased interest not only from these two market participants, but also from beneficial owners. CCPs will allow borrowers to capture netting benefits and will reduce the risk weighting applied to agent lenders' indemnified transactions. As the securities finance industry recognises the benefits of a CCP model, EquiLend has partnered with Eurex Clearing to facilitate CCP access for our client base. Our clients will be able to make use of their existing infrastructure to route transactions to Eurex Clearing's Lending CCP. As this new route to market emerges, DataLend is poised to capture transactions executed on CCP platforms in addition to traditional bilateral trades.

Wilson: Beneficial owners are expressing an interest in the benefits and how they will impact on them. The benefits are more obvious for borrowers and agents but are less clear for beneficial owners. Beneficial owners would want to understand whether this will result in higher revenue or lower risk. Given the current product, market, and collateral coverage from CCPs, there is only a relatively small amount of business that could be transacted, but further increase would be reliant on other factors all being aligned. That being said, given the regulations and rules that are upon the industry, CCPs can play a part of the changing landscape. Going on that journey as they expand and build out capability is a positive development.

Saunders: We continue to hold client discussions that primarily focus on the role of CCPs as counterparty, as well as on the protection of client assets in the event of a default. Though such conversations have become more frequent, at this time we still do not see CCPs occupying a central role within the US marketplace anytime soon.

That said, we intend to closely monitor new developments on behalf of our clients, with the belief that ongoing discussions will be beneficial to the markets as a whole. The bottom line is that many clients will be required to conduct a complete review of their lending programmes, including what is permitted under their existing charters, guidelines or mandates, before any such changes can occur. **SLT**

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- COLLINE ELECTRONIC MESSAGING - automates **the interaction between financial institutions on** their margining requirements (margin calls, partial **and full dispute notification, real-time visibility of** counterparty actions, interest statements, and collateral substitutions) thus reducing operational risk.

Young blood schools established markets

With securities lending revenues down in some major markets, Chris Benedict of DataLend examines the growth seen in emerging markets in 2015

Last year was a tough one for generating revenue in some of the established securities lending markets. While the US and Canada both saw revenues increase, Europe's 2015 securities lending revenue was down 12 percent, from $3.2 billion in 2014 to $2.83 billion in 2015. This decline was led in part by France, whose revenues dropped by 35 percent, from $896 million to $586 million. Spain, Portugal, Belgium and the Netherlands also saw securities lending revenues decline in 2015. Across the board, the decline in revenue was driven by both lower fees and loan volumes.

With increased regulatory requirements, balance sheet pressures and thinning profit margins, are there still areas of potential revenue growth within securities finance? When looking at emerging markets, the answer is resounding positive.

Brazil, the largest securities lending market in South America, experienced an increase in average loan balance from just below $2 billion in the beginning of 2015 to approximately $2.6 billion today, representing a solid 30 percent increase for the year. Volume-weighted average fees to borrow Brazilian assets climbed 190 percent, from approximately 84 basis points (bps) in the beginning of last year to 246 bps at the time of writing.

A key driver of demand was Brazilian sovereign debt, where average fees to borrow increased from a low 29 bps to 87 bps by the end of 2015. The average on-loan value for Brazilian sovereign debt was approximately $1.42 billion, while utilisation for this asset class averaged 31 percent for 2015.

Brazilian equities were also in great demand last year with an average on-loan value of $1.58 billion, a 29 percent average utilisation and volume-weighted average fees of 291 bps for 2015.

Although a smaller market than Brazil, Chile has also seen some impressive growth in the securities lending market in terms of both daily on-loan value and fees. Chile started 2015 with on-loan balances of just over half a billion dollars. By year-end, balances increased to nearly $2 billion on loan, representing an increase of 300 percent. Fees to borrow Chilean securities also took off during the summer of 2015, rising from 22 bps to a little over 80 bps at the time of writing. Agency debt was a catalyst of this demand—fees to borrow agency bonds rose from 19 bps in early 2015 to 88 bps today. Chilean agency debt saw a daily average on-loan balance of just under $900 million and an average utilisation of 31 percent last year.

In Mexico, on-loan values fluctuated between $2.3 billion and $4 billion to yield an average daily on-loan balance of approximately $3.04 billion for the year. Fees to borrow Mexican securities rose steadily throughout 2015, from 27 bps in early January to 47 bps in late December.

Other smaller but still hot markets in South America include Venezuela, which traded at a yearly average of around 101 bps last year, and Argentina, which traded at an average of around 127 bps.

In Asia, daily on-loan values for Thai securities grew from $1.28 billion in the beginning of 2015 to just over $1.5 billion at the time of writing. Fees also followed suit, climbing from a little over 100 bps early last year to 145 bps today. This was driven mostly by equity demand, as there is very little lending in Thailand's fixed income market.

Taiwan also experienced solid loan growth in 2015 as on-loan volumes grew from just under $7 billion in January to $8.2 billion today. Fees were a bit choppy for the year, starting out around 185 bps and dropping to a low of 144 bps by July. Since then, fees have rebounded to 180 bps, offering solid securities lending revenue potential. Like Thailand, the balance and fees are predominately reflective of the equity market, given very low volumes in the fixed income securities lending market.

Turkey also shows some revenue opportunities. While the daily on-loan value has remained relatively flat for the last year at around $2 billion, fees to borrow Turkish securities saw steady growth from 89 bps in January 2015 to 167 bps at the end of the year. The increase in fees here was also primarily due to the equities market, which had an average daily on-loan balance of $1.2 billion and average fees to borrow of 197 bps for 2015. Sovereign debt was also a factor, which started the year trading at 19 bps but ended it at just under 50 bps.

While there appear to be some great revenue opportunities in these countries, there are other factors to consider in emerging markets such as borrowing restrictions, operational or settlement issues, margin rules, a low number of lendable securities and liquidity risk. But despite these challenges, it seems that the appetite to increase lending activities in emerging markets is on the rise. SLT

Figure 1: Percentage of Brazilian Securities On Loan by Fee Band, January 2015 to January 2016

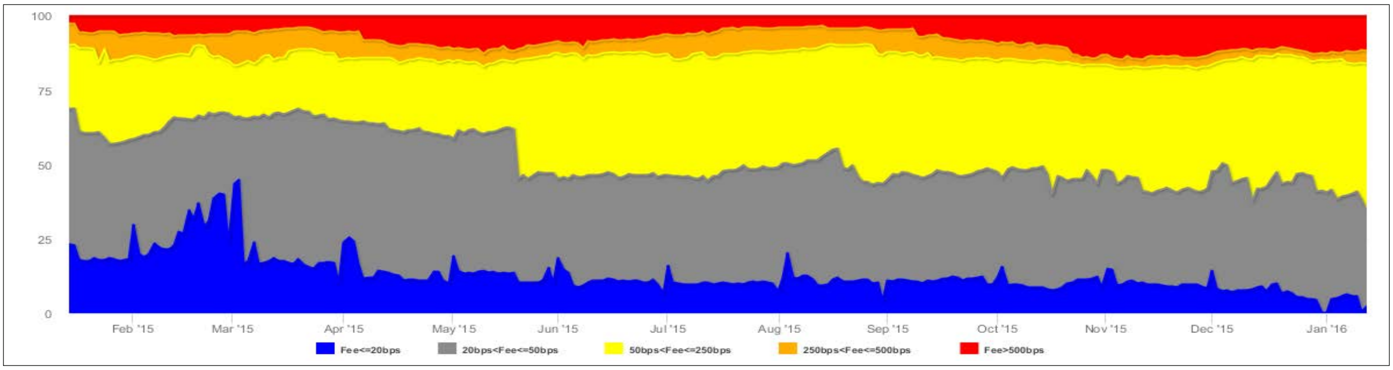
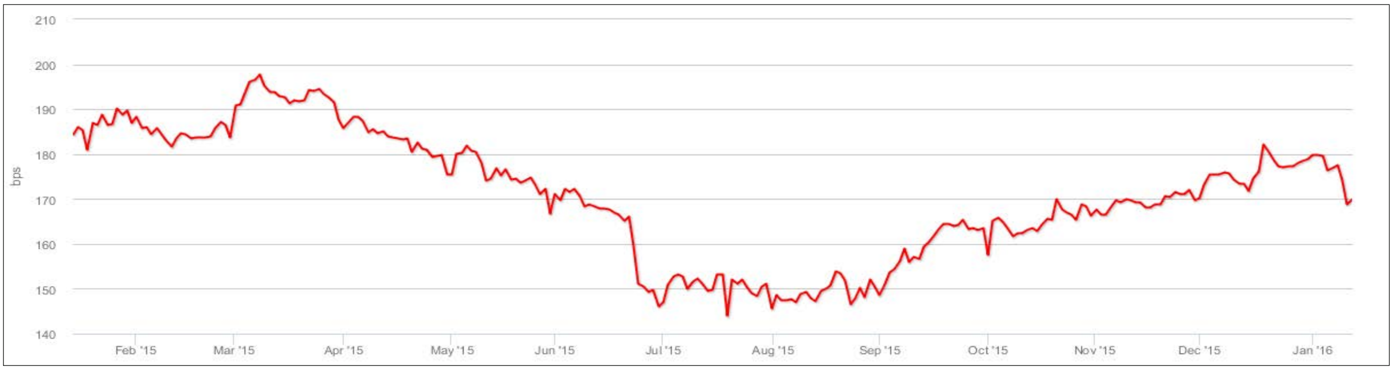
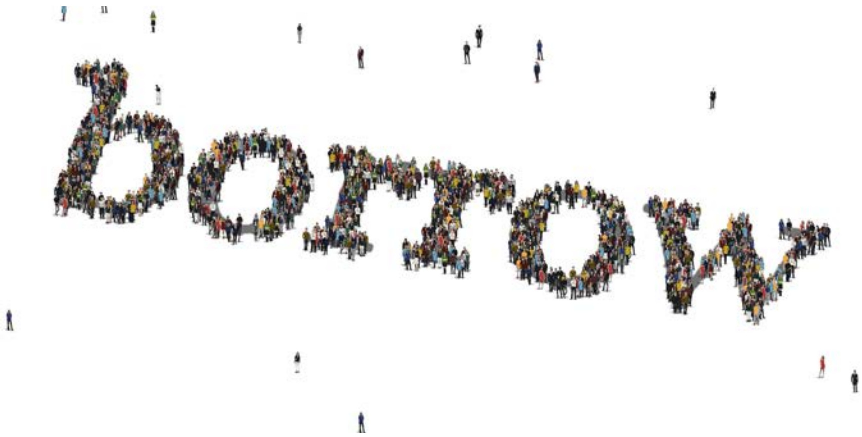


Figure 2: Volume-Weighted Average Fees to Borrow Taiwanese Securities, January 2015 to January 2016



A key driver of demand was Brazilian sovereign debt, where average fees to borrow increased from a low 29 bps to 87 bps by the end of 2015

Chris Benedict, Director, DataLend



Short sellers hold steady after stellar 2015

Appetite to sell stocks short has showed no signs of abating in the new year, with demand to borrow shares up by more than 14 percent in the past 12 months. Markit analyst Simon Colvin reports

Last year witnessed a surge in short selling activity as the economic climate saw short sellers add to their positions across major global markets. The ongoing nature of the Chinese slowdown and commodities slump also ensured that the top short strategies carried strong momentum into the end of the year, with shorting activity peaking in the closing weeks of 2015.

From a performance point of view, the year proved very fruitful for short sellers as the 10 percent of shares that short sellers were the most willing to pay up for underperformed the rest of the market by a wide margin over 2015. The small minority of stocks that make up the highest conviction shorts in the US underperformed the market by a staggering 25.7 percent over 2015, according to the Markit Research Signals Implied Loan Rate factor.

Short sellers in Europe and Asia also enjoyed a profitable year as their high conviction positions managed to underperform the market by 12 and 7 percent, respectively.

US returns best on record

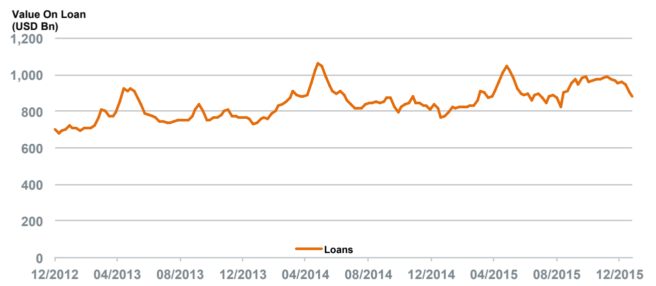
Perhaps most surprising of all is the fact that the strong underperformance of the high conviction US short positions over last year makes 2015 the best ever year for short sellers since the genesis of the Implied Loan Rate factor in 2007.

Even the financial crisis of 2008 proved less fruitful for high conviction shorts, when this group of shares only underperformed the market by 18.5 percent. Surprisingly, the least most profitable year for US short selling was 2011, when the most expensive to borrow 10 percent of US shares underperformed the rest of the market by 23.8 percent.

Shorts show no sign of slowing down

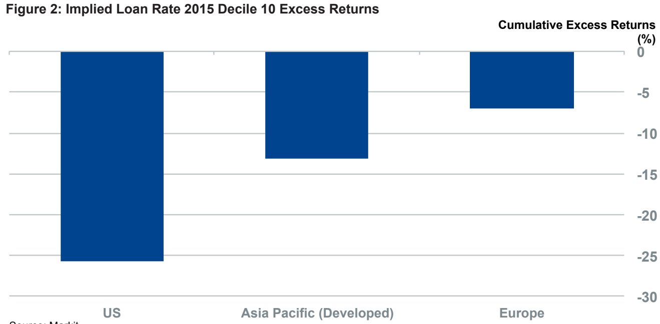
The appetite to sell shares short also shows no signs of slowing down in 2016 as last year's macro catalysts for market volatility have shown little signs of subsiding. This increased propensity to sell short looks to be playing well into the hands of the securities lending industry, as the current value of equities now out on loan is more than $100 billion higher currently than at the same time a year ago, a healthy 14 percent year-on-year increase. **SLT**

Figure 1: Global Equity Value On Loan



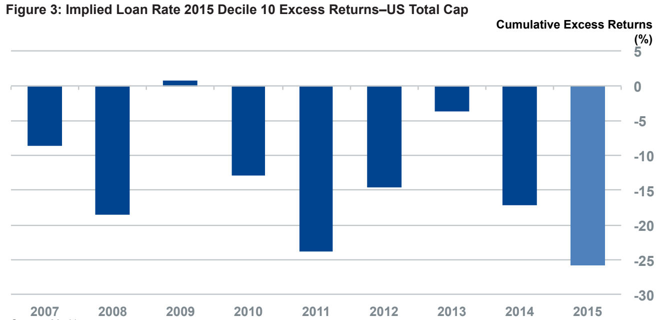
Source: Markit

Figure 2: Implied Loan Rate 2015 Decile 10 Excess Returns



Source: Markit

Figure 3: Implied Loan Rate 2015 Decile 10 Excess Returns–US Total Cap



Source: Markit

Industry **Events**

20th Clearstream GSF Summit

Date: 26 - 28 January 2016

Location: Luxembourg

www.clearstream-events.com

Clearstream's Global Securities Financing Summit will celebrate its 20th anniversary in 2016. This edition will be held on 27 and 28 January 2016 in Luxembourg. Visit the website for more information.

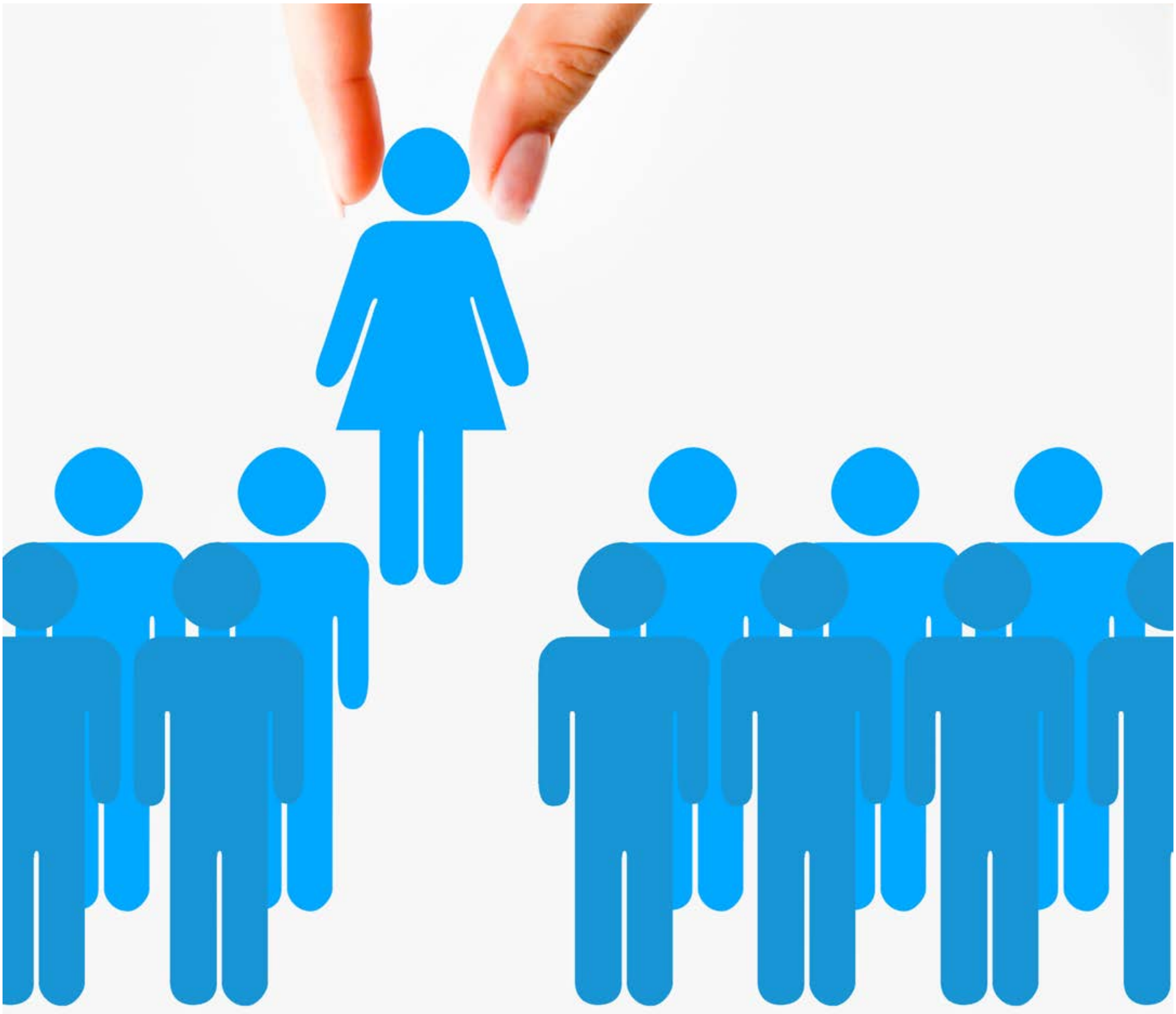
IMN's 22nd Annual Beneficial Owners' International Securities Lending & Collateral Management Conference

Date: 03 - 05 February 2016

Location: Arizona

www.imn.org

In such a dynamic market, beneficial owners need to fully understand where the industry is heading, the implications for their securities lending programmes, and what it is that they need to be doing to position themselves for continued success in the new world order.



Comings and goings at RBC Capital Markets, DataLend and more

The head of US securities lending at RBC Capital Markets, **Bobby Colon**, has retired. Colon, who joined RBC Capital Markets in 2006, has more than 30 years of experience in the securities lending industry.

He also held the role of assistant treasury at the Securities Industry and Financial Markets Association.

Colon said: "In my retirement years I look forward to spending more time with my family, playing a little golf and finding new adventures. I am so grateful for all of the many friendships that resulted from my time in this industry, ones I believe will last a lifetime."

CloudMargin has appointed **Steven Husk** to the newly created role of executive chairman.

In his new position, Husk will lead CloudMargin's collateral management services and drive the company's plans for domestic and international expansion.

Husk boasts more than 35 years of experience working at some of the industry's leading firms.

Before joining CloudMargin, he was CEO of FRS Global, where he provided risk-management and regulatory compliance solutions to the financial services industry.

He is also an angel investor and independent director who has worked primarily in the financial services software space.

"I am hugely excited to join a company that has become one of the best growth stories of 2015, and to be given the opportunity to expand on the current success CloudMargin are experiencing is one I could not decline," said Husk.

"CloudMargin are the only collateral management SaaS solution on the market that allows users of derivatives to meet their new, post crisis objectives set against an environment saturated in regulatory demands. We are now ready to position ourselves

as the premium solution for the financial industry's collateral management needs."

Andy Davies, CEO of CloudMargin, added: "I am thrilled that Steven Husk has joined CloudMargin. Given the raft of new collateral-related regulation about to be implemented, there is a material gap in the market for a cloud-based collateral management solution, thus perfectly positioning CloudMargin to meet the requirements of these market participants."

Nancy Allen joins DataLend from Northern Trust

DataLend, the securities finance market data division of EquiLend, has appointed **Nancy Allen** as product owner, effective immediately.

Allen will be based in New York and offers more than 15 years of experience in the securities finance market across multiple client types, regions and roles.

As DataLend's product owner, Allen will be responsible for determining and delivering the product roadmap, including enhancements and new features, and managing its team of business analysts and technical staff.

Allen joins DataLend from Northern Trust, where she was most recently senior vice president and head of international fixed income securities lending trading, based in London.

She has also held various positions in securities finance at State Street and Deutsche Bank.

Allen said: "As a former DataLend client and user, I have been very impressed by the product's growth since launching in 2013. I am excited to lead the talented team behind DataLend as we continue to improve the securities finance industry's leading market data provider."

Brian Lamb, CEO of EquiLend, added: "Allen has a robust knowledge of the global securities finance market. With her wealth of experience in the industry, we are confident that DataLend will be better than ever under her direction."

"Allen shares our belief that clients are our top priority, so we anticipate her exceeding expectations in meeting the data needs of our clients and the industry."

Deutsche Bank has added **Andrew Pettit** to its agency securities lending in the Americas.

Andrew Pettit, who has more than 15 years of securities financing experience, is based in New York

Pettit joins as a director and platform enhancement specialist, focusing on product innovation.

Pettit, who has more than 15 years of securities financing experience, will be based in New York and will report to Anthony Toscano, co-head of agency securities lending in the Americas.

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Before joining Deutsche Bank, Pettit was an executive director in bank resource management sales and marketing at Morgan Stanley.

Prior to that, he was head of business development at Brown Brothers Harriman's global securities lending unit.

Deutsche Bank's agency securities lending programme is part of its global transaction banking business, which includes non-custodial securities lending, portfolio financing and collateral management.

"Pettit's deep and diverse experience in securities finance will further our ability to meet the sophisticated needs of our clients," commented Toscano.

"We are pleased that Pettit has joined the team as we continue to grow and invest in our agency securities lending programme." **SLT**