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Finadium publishes best execution guidelines

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Any moderately opaque market falling under the heading of shadow banking is a prime target for regulators, according to Josh Galper, managing principal at Finadium. And securities lending is no exception.

Finadium recently published guidelines to achieve best execution in the market and chief among them is that one size does not fit all, while even the definition of "best execution" becomes complicated once multiple sizes are taken out of the fitting room.

Rather than a single data point, the firm believes that analysing a series of metrics is the best method for evaluating the performance of a programme, agent or asset class in the context of the lender. A mutual fund board, pension plan operator, insurance company, endowment or municipality can then conclude whether best execution has been achieved.

One point of contention is when lenders look at purely quantitative data to measure performance. For example, judging a third party benchmark report with either poorer or better rates compared with the market average without fully comprehending the reasons behind the results.

Multiple factors influence such results and affect returns, explained Galper, as individual mandates from beneficial owners' boards may place restrictions on programmes such as what proportion of securities can be loaned out. Another common scenario which causes mismanaged expectations is the confusion between collateral returns and returns from the intrinsic value of the loan itself.

The Finadium methodology for identifying best execution in securities lending recognises the unstandardised attributes of this market and provides a means for evaluating risk versus return.

"It has been said many times that securities lending and collateral management need the same level of supervision as other investment products, however this is still not always taken to heart by beneficial owners " Galper noted. "In today's environment where it can pay to be risk averse, securities lending can be a profitable and successful activity but it is also important to manage the potential monetary and reputational risks associated."

NEWSINBRIEF

Short covering not driving share price - Data Explorers

Though short sellers have been covering positions in the recent market upturn, it has not necessarily driven share prices higher, accroding to research from Data Explorers.

By analysing the 50 most and least shorted stocks and subsequent price movements, the analytics firm challenged the view that the surge in the S&P 500, rising 6.1 per cent since the start of October, was due to short sellers being squeezed out of positions.

"Short interest has retreated slightly in the last couple of weeks. However, this decline does not point to a short squeeze as the shares which have seen the greatest price increase actually had a below average short interest coming into the quarter and the shares which saw the greatest short covering underperformed the market," wrote Data Explorers.

BlackRock sees securities lending lift revenue

BlackRock has credited securities lending revenue and advisory and administration fees for an increase in Q3 revenue.

Third quarter 2011 revenue of $2.2 billion increased $133 million, or six per cent, from $2.1 billion in the same quarter the previous year, while third quarter net income of $595 million is an eight per cent lift from a year ago but a drop of four per cent quarter on quarter.

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BlackRock sees securities lending lift revenue

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"Investment advisory, administration fees and securities lending revenue of $1.9 billion in third quarter 2011 increased $155 million, or nine per cent, from $1.8 billion in third quarter 2010. The increase in fees reflected growth in average long-term AUM which included the benefit of net new business, partially offset by a decline in fees from cash management products due to lower average AUM," wrote BlackRock.

Long-term AUM of around $3.0 trillion decreased $308.3 billion during the quarter, largely driven by market and foreign exchange declines of $298.7 billion. Cash management AUM of $244.7 billion declined one per cent.

Naked short sale ban "diluted" - European parliament

A short selling regulation deal has been reached by the European parliament in a bid to beef up standards and requirements.

Naked CDS trading will be banned if the agreement is ratified next month and enters into force, predicted in November 2012. This is considered a major victory by regulators who fought to put an end to sovereign debt speculation by entities that do not own the related bonds.

The sole exception to the proposed naked CDS ban is an option for a national authority to lift it temporarily in cases where its sovereign debt market is no longer functioning properly though the circumstances under which this is allowed are heavily prescriptive.

Also key to strengthening the Commission proposal is stepping up reporting requirements. For example, supervisors would be informed of large short positions when this position accounts for 0.5 per cent of the issued capital.

The MEPs' wish that naked short sales would no longer be possible for more than one day was however diluted. The hard "locate and reserve rule", whereby a trader must not only notify from where it plans to borrow the shares in question but must also have a guarantee that it will indeed be able to borrow them, was diluted, requiring the trader to locate and have a "reasonable expectation" of being able to borrow the shares from the located party.

MEPs from groups sponsoring the deal also managed to preserve the powers of the EU's financial markets watchdog, ESMA, in particular to restrict short selling, as an arbiter of a national authority's wish to introduce measures to address exceptional situations, and also to require other authorities to introduce exceptional measures to deal with difficult situations.

"The new powers for ESMA will allow for better co-ordination at the EU level in times of crisis", said MEP Pascal Canfin (Greens, FR), adding however that "It would have been better had ESMA had similar powers over decisions relating to sovereign debt but the member states refused".

Short sellers in Asia 'bet on slowdown'

Short sellers in Asia have increased their exposure to the sectors expected to get hit by a global slowdown, according to Data Explorers.

Securities lending data show that stocks within the materials, retail and real estate sectors in Asia (excluding Japan) dominate the list of companies seeing a fresh annual high in short interest.

"It is interesting to note that market sentiment in Asia has fallen from its peak at the beginning of the year. Short interest has risen to $98 billion - a level not seen since the start of 2009 - up from $80 billion at the start of January. Yet short interest stands at only one per cent of the total Asian shares," wrote Data Explorers.

Meanwhile, the analytics firm's Long Short Ratio for Asian equities has fallen to 7.2, meaning that longs outnumbered shorts by just over seven times, well down on the annual average of 10.

Lightspeed to provide prime brokerage services

Lightspeed Financial has expanded into prime brokerage with the launch of Lightspeed Institutional, which will offer a specialised prime brokerage platform for professional investors.

In addition to front-end manual and automated trading solutions, it provides a sales trading desk for execution services, technology solutions, custody, clearing, securities lending, and portfolio reporting. Lightspeed Institutional also delivers robust pre-trade risk management and real-time risk monitoring.

Stephen Ehrlich, CEO at Lightspeed Financial, said, "The launch of our prime brokerage business is a necessary next step in our strategic growth plan aimed at delivering the most complete and customisable suite of trading technology and brokerage services across asset classes to professional traders."

BNY Mellon launches Solvency II solution

BNY Mellon has launched a new data management solution to meet the European insurance industry's Solvency II asset data reporting requirements.

The new service, built around Eagle PACE, Eagle Investment System's data management platform, provides Pillar 3 Quantitative Reporting Templates (QRT) reporting. It also supports insurance companies as they negotiate the data governance and data quality hurdles imposed by the new regulations.

The service meets key client needs around Solvency II asset data requirements in respect of:

- Gathering and validating the data from the insurer and the insurer's partners using industry standard templates
- Data enhancement via BNY Mellon's own vendor feeds and the insurer's own management information
- Data consolidation and reporting as specified in the regulations.

Frank Froud, head of Europe, Middle East & Africa (EMEA) for asset servicing at BNY Mellon, said: "To date, the focus for insurance companies has rightly been the calculation of the Solvency Capital Requirement and how this may affect future business. Attention is now turning from Pillars 1 and 2 to Pillar 3, and in particu-

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lar the contents of the QRTs. The QRT data requirements are extensive, spanning enterprise, portfolio and reference data typically housed on a multitude of systems within both the insurers and their suppliers' organisations. Not only must this data be gathered and consolidated, it also has to be enriched if it is to comply with the strict data quality requirements stipulated by Solvency II."

John Legrand, managing director, Europe, Middle East & Asia-Pacific at Eagle Investment Solutions, said: "Our solution provides insurance companies with a centralised approach to data quality management that goes above and beyond the requirements set out in the Directive. Eagle's proprietary data-centric technology means we can automate the process and provide clients with complete, accurate, and transparent data to support greater operational effectiveness and stronger risk-based decision making in the context of Pillars 1 & 2."

Paul Traynor, head of insurance, EMEA at BNY Mellon, said: "Market Risk comprises two-thirds of a life insurer's Solvency Capital Requirement. So the creation of a strong data governance model around asset data collection is of paramount importance. When you take into account other complicating factors, such as investments in alternatives and repos as well as securities lending activity, then it is clear there is a definite need for a robust, data-centric solution to meet Solvency II's asset data collection requirements."

Citi to provide securities lending to AGF

Citi Global Transaction Services (GTS) has announced that it has recently implemented securities lending services for AGF's retail mutual funds in Canada. This represents an expansion of the company's existing long-term relationship with AGF, which includes fund administration, fund accounting, transfer agency and custody services.

"Our relationship with AGF is a key element of our Global Transaction Services franchise," said Bob Wallace, securities and funds services' head for the North America Region. "The addition and implementation of a securities lending component with such a first-class organisation is a notable business milestone for us as we continue to grow our Securities and Fund Services business in Canada."

Using its OpenLend platform, Citi provides securities lenders customised service to enhance their portfolio performance by delivering an open architecture that provides access to agency, third-party, hybrid and exclusives lending.

UK collateral upgrade trade eyed by FSA

The Financial Services Authority (FSA) is considering enacting guidelines on the collateral upgrade trade after increasing activity has caused concerns over macroprudential risk.

A recent FT article claimed that sources within the financial services industry reported blocked "liquidity swap" transactions – which may include stock (securities) lending, repo transactions or sale plus total return swap - however, an FSA spokesman denied being aware of any blocked transactions since actions on guidance are still being put in place and the UK regulator continues to consult the industry on proposals, at the same time it is the FSA's practice to not comment on supervisory actions with firms.

In stock lending, gilts, or UK government bonds, are lent by an insurer for a significant period in return for a fee and collateral. Legal ownership of the gilt passes to the borrowing bank counterparty - in the event of the bank counterparty defaulting, the insurer has recourse to the collateral.

"If structured and operated correctly, valuation, margining and over-collateralisation should protect the insurer against loss in the event of a 'fire-sale' of the collateral. To the extent there is insufficient collateral the insurer will have an unsecured claim against the bank counterparty," the FSA wrote in its guidance consultation.

The main areas of concern for the FSA are in the mechanics of risk management within organisations participating in liquidity transformation – seemingly trading up asset-backed securities (ABS) as this structured product is mentioned in the guidance consultation - and what the potential impact might be on the wider economy if the practice becomes more common.

This is quite likely to become a reality, as most industry experts across the banking, insurance and pension fund industries are expecting the collateral upgrade trade to become a major driver of securities lending activity since global regulations pushing OTC transactions on exchange will substantially increase the demand for high quality collateral to post to a CCP against derivatives trades.

Irving Henry, director of Prudential Capital and Risk at the British Bankers' Association (BBA), says that the FSA proposals are in their infancy but that the regulator needs to spend more time looking at a wider variety of transactions and become more comfortable with the way that different market participants approach the practice.

"There was very much a feeling [during the consultation] that insurance companies need to be protected from banks and whether the governance of risk at the insurance companies was up to scratch," he says. "But [insurance companies] felt better able to hang on to these types of [riskier] assets because they tend to be long investors and they are trying to get some additional yield which they are not able to do holding a shedload of gilts."

Gilts fit better with banks which need the immediate liquidity, while insurance companies feel able to sit out stresses by holding onto the assets for a longer period of time, he adds.

Another sticking point for the FSA for liquidity swaps was on the issue of intragroup transactions, meaning that the insurance company and bank are part of the same Group. Henry explains that currently, those transactions are subject to regulatory scrutiny to ensure risks are captured properly but also tax authorities and auditors require transactions are done on an arms length and transparent basis.

Meanwhile, disclosures on stock lending in mutual funds is also a reported activity, something commonly understood by mutual fund trustees. "There is something to be said about treating

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customers fairly and that the churning of a portfolio ought to be disclosed more widely than it is and there ought to be a better spread of the fees earned from such transactions because they accrue to the manager rather than to the investors," Henry said. "But it would have been helpful if the FSA could have spent a bit more time talking to participants and giving us some clear conclusions based on a pool of transactions…so we can start thinking about how this plays into financial stability."

Apart from banks feeling pressured by Basel III and the capital requirement directive CRD IV, the insurance fund industry is facing regulations under Solvency II, which could make these transactions "uneconomic" according to the FSA.

"These rules are being developed in isolation and that silo [mentality] leads to issues not being addressed, because they fall through the gaps, but also unintended consequences," Henry says, adding that if banks cannot swap riskier pools of assets with pension funds and insurance companies, it is not clear where those assets will go to relieve pressure on balance sheets.

NSE to deliver securities lending rules in December

Rules on securities lending are expected to be issued in December by management of the Nigerian Stock Exchange (NSE) in a bid to mature the capital market, according to media outlet This Day Live.

CEO of the Asset Management Corporation of Nigeria (AMCON), Mustapha Chike-Obi, who was involved in developing the rules, spoke to This Day at the fall meetings of the International Monetary Fund (IMF) and World Bank in Washington.

According to Chike-Obi as reported by This Day, the rules and regulations that would guide securities lending in Nigeria were already concluded and were being forwarded to the national regulator of the capital market, Securities and Exchange Commission (SEC), Nigeria for approval.

Dodd-Frank implementation in sight at RMA conference

This year's Risk Management Association (RMA) conference, which ran from 10 to 13 October in Naples, Florida, is the last before the Dodd Frank Act is to be implemented and reviews are mixed on the sweeping regulatory reform which is shaking up traditional securities lending markets' business models.

Almost as if on cue, the 300-page Volcker rule was released during the week by five coordinating regulatory bodies in the US and, as expected, securities lending desks which provide "bonafide liquidity management" are exempt from the definition of a trading account.

But it is the cumulative impact of legislation, such as Dodd Frank and Basel III, on the securities lending industry's bottom line that is the concern. So too, is the increasing amount of workload for the RMA and the Securities Industry and Financial Markets Association (SIFMA) as more regulations keep coming and more Dodd-Frank rules are yet to be finalised before the 12 July deadline next year.

"There are a lot of mandates that the Securities and Exchange Commission and Federal Reserve feel empowered to execute. RMA and SIFMA are working on five to seven mandates when last year we were working on three and that is a lot to keep up with, this is an unprecedented time in history," said Christopher Kunkle, managing director at RMA.

Additionally, cost of capital and leverage charge issues are being contemplated at the Federal Reserve (FRB) level and have to either be worked through or better understood, he says.

"If I am indemnifying an agent lender from broker-dealer default, I basically have access to the collateral…if I have to cover the claim…[and] that portion goes on balance sheet…let's just say banks don't want a business that has a high cost of capital," he said.

"If things don't change, rates stay flat, earnings will stay flat, but we have to get through all this regulation and help everyone understand how it does and doesn't affect [the securities lending market]…I think the regulators will do their best to deliver Dodd-Frank on time, but what will it look like?" he added.

Some future-forward topics were discussed as well. Backed by research, market participants questioned whether the SEC might begin to consider allowing equities as collateral in the US market as the industry faces increasing collateral costs and stiff competition from Europe, where the practice is common. But Kunkle thinks it is doubtful the SEC will take a look before Dodd-Frank is out of the way and the regulator takes a breath.

Meanwhile, a CCP panel highlighted the chasm between lenders and borrowers on the entry of clearing houses, indicating there is more work to be done. Although there was widespread agreement among agent lenders and borrowers that some transactions should go through a CCP, the vast majority of agent lenders did not believe mutualisation decreased risk while borrowers veered the other way. At the same time, there was general agreement that CCP transactions should have a lower regulatory capital requirement.

Market bounce due to short covering - Standard Chartered

The recent market bounce is a consequence of short covering, says Standard Chartered. "The approach of European policy makers is still fraught with significant execution risk and the recent focus on bank recapitalisation still deals with the symptoms rather than the cause though liquidity injections from central banks globally could lift the market temporarily," the bank wrote in a recent report.

The Bank of England announced a second round of so-called quantitative easing to the tune of £75 billion ($118 billion) while rumours of further bond buying from the Federal Reserve have been circulating in various media reports. Meanwhile the European Union may be increasing the leverage power of the EFSF after Slovakia ratified expansion plans.

"We prefer to use such a bounce to reduce illiquid risk positions rather than to add positions," Standard Chartered noted. Still the bank does forecast that a new recession will be avoided though there is no doubt that the risk has risen.

"We expect confidence to pick up slowly as economic data continues to defy the worst fears and Europe gradually puts in place more measures to strengthen its banks and weak sovereigns," it wrote.

HazelTree launches new Treasury Suite

HazelTree Fund Services has launched the next generation of its Treasury Suite product; the first Treasury system embedded with Form PF.

HazelTree designed this to help hedge fund executives better navigate through the new era of oversight and regulation led by the Dodd-Frank Act. This next generation of the Treasury Suite has been extended well past the Dodd Frank compliance features by including new portfolio margin functions, automatic access to institutional money market funds, automated swift wire transfers, integrated swift service bureau, expanded securities financing market data, as well as its breakthrough Form PF filing feature.

The announcement was made by Stephen Casner, CEO of HazelTree.

“As a recognised leader in treasury management,” stated Casner, “HazelTree has taken on the responsibility of helping treasurers at hedge funds increase their fund’s performance through rate and margin tracking, improve risk management by detailing counter party relationships, streamline operations through better reconciliation services and now directly manage compliance by creating an integrated electronic Form PF filing feature.”

HazelTree clients now have the advantage of filing their Form PF requirements directly from HazelTree’s Treasury Suite product. This functionality, developed by HazelTree in conjunction with Advise Technologies, coalesces all financing, performance, risk analytics, positions, AUM, exposures, fund and investor information to generate a complete PF Workbook, which can then be filed directly with the SEC or furnished to a compliance advisor, depending upon client preference.

“We listened carefully to our clients and Dodd-Frank is clearly an issue that is central to their compliance requirements” said Casner. “So we designed our new Treasury Suite to directly address their needs in this area. With compliance deadlines looming just around the corner, this is not just a timely but an efficient answer to a complex and costly challenge all private funds face.”

Hong Kong regulators deny market declines a result of short selling

There is no indication that recent declines in the Hong Kong stock market have been caused by short selling activities, said China’s capital markets regulator, the Securities and Futures Commission (SFC).

“Short selling is a trading and hedging tool commonly and legitimately used by a range of market participants. It is not unusual to see the level of short selling increase significantly in the market environment we have been experiencing in recent months,” said Ashley Alder, CEO of SFC.

Stock markets around the world have seen significant downward adjustments and increased volatility in recent months against the background of an uncertain global economic outlook and the eurozone sovereign debt crisis, however Alder did note that the SFC will not hesitate to take immediate action to deter any manipulative or abusive short selling practices.

“Extreme volatility has reflected global concerns centred on an evolving financial crisis which started three years ago, and which is now centred on sovereigns and exposed banks, particularly in the eurozone,” he added.

In relation to the market rally in the last two days, Alder pointed out that markets are currently “very sentiment driven”.

“We can see this from the market rebound following reports of greater political resolve in Europe to address the debt crisis, and news of further market stimulus by the Bank of England and the extension of unlimited liquidity by the European Central Bank to Eurozone banks,” Alder notes.

He reiterated that Hong Kong has a robust short selling regulatory regime that is more stringent than most overseas markets, and that the SFC will be introducing legislation shortly to implement a short position reporting regime to further enhance the transparency of short selling activities.

Only covered short sales are permitted in Hong Kong and both the seller and broker are required to confirm that the short selling orders were covered before executing the transaction while short selling orders must be flagged when submitting to the Stock Exchange of Hong Kong (SEHK) for execution.

In addition, only liquid stocks are permitted by the SEHK for short selling and the uptick rule imposed by the SEHK requires that a short sale cannot be made below the best current ask price. Furthermore, the SEHK requires compulsory buy-in for failed trades if sellers cannot deliver the stocks for settlement.

Heavy shorts in retail sector, miners ahead of earnings season

Data Explorers analysis shows increased short selling activity for miners and retailers ahead of what is predicted to be another disappointing earnings season.

Leading the miners for earnings reports is Aluminium producer Alcoa, which had its recovery stall when aluminium prices fell in a broad-based commodities sell-off.

As share prices continued to fall, shorts returned after having covered positions in the second quarter, while a convertible bond in issue may spur arbitrage trading, Data Explorers reports.

Uranium Energy, meanwhile, has seen historical heavy shorts recently and, though institutional investors which lend have expressed positive sentiment and are increasing holdings amid the miners’ progressing expansion plans, two-thirds of the lendable supply is out on loan.

On the retail side, the US’ sector has become increasingly short evidenced by the decline in the Data Explorers’ Long Short Ratio. It peaked at nine in April and has since fallen to 6.75, meaning that longs outnumber shorts by just under seven times.

“This increased negative sentiment is similar to levels seen a year ago and the six month decline represents the longest fall in the retail ratio for over three years,” Data Explorers wrote.

In contrast to the US, the Long Short Ratio for the European retail sector has increased from its annual low of 4.7 in May to 6.1.

UK retailers are seeing high levels of short interest, with Next topping the list of FTSE 100 companies with the greatest percentage of stock on loan.

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Short Exposure	80%	75%	110%	100%	85%
Avg. Credit Cash Balance	15%	10%	10%	10%	5%
Avg. Debit Cash Balance	10%	5%	15%	15%	12%
% Longs Hard to Borrow	10%	5%	7%	7%	5%
% Shorts Hard to Borrow	30%	30%	25%	20%	15%
Typical Treasury Impact on a Fund					
Cash Management	$125,000	$125,000	$375,000	$750,000	$750,000
Stock Loan Management	$900,000	$1,000,000	$2,100,000	$3,990,000	$19,800,000
Stock Borrow Management	$1,180,000	$2,212,500	$4,331,250	$6,900,000	$8,415,000
Total Performance Increase	$2,205,000	$3,337,500	$6,806,250	$11,640,000	$28,965,000
Impact in Basis Points	44.10	33.38	45.38	38.80	48.28

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Risk and reward

As collateral management becomes an even more integral part of the market, J.P. Morgan's senior team speak to SLT about how the market is changing

ANNA REITMAN REPORTS

Fresh off successful technology enhancements to meet U.S. tri-party repo reform deadlines, J.P. Morgan Worldwide Securities Services (WSS) is eager to complete market reforms and help clients grow their tri-party business. And, though the impact of global regulations injects uncertainty, some things are certain – collateral management is going to be a big deal.

In this interview with SLT at October's Risk Management Association (RMA) conference in Naples, Florida, J.P. Morgan's representatives at the event talk about the enterprise-wide approach to collateral management taking shape and how it might affect the future of the securities lending market.

Just as Anne Sylvester joined WSS, collateral management was thrust into the spotlight. She reckons it was good timing.

Sylvester is the Americas head of client management and technical sales for Financing and Market Products and, in this role based in New York, she works in partnership with product teams across J.P. Morgan's business lines while maintaining dialogue with clients about industry developments.

"To me, it's really pretty exciting, because collateral is the centre of all of the reform requirements. Collateral management has gone from being a sleepy business to being at the forefront of investors' and dealers' minds," Sylvester says.

That is because a number of global regulations pushing for central clearing of most OTC derivatives have made clients have to think about the future in a new way – how are they going to post margin and to whom? At least, those clients not in total denial.

Sylvester admits that there are varying levels of engagement by swap dealers while Dodd Frank rule writing continues, particularly as the impact of a combination of global regulations remains hazy. Still, she sees an increasing need from investor clients to be walked through solutions being developed, though at the moment there seems to be little sense of urgency in implementing strategic changes.

"Swap dealers are assessing their own collateral needs going forward. They are focused on how their financing needs will change in addition to how they will accommodate their client's needs," Sylvester says. "We've been working with our beneficial owners to help them understand how the new collateral requirements will impact them. For example, how will the new rules affect their performance, their infrastructure needs and their potential need to hold high quality collateral?"

It is precisely this need for transformation to post high quality collateral accepted by CCPs that is plaguing some and creating opportunities for others.

Securities lending, though not in the trade flow, is one route broker dealers take to upgrade collateral and, though it is early days, beneficial owners are looking at the opportunities offered by lending as a consequence of that increasing demand to enhance returns.

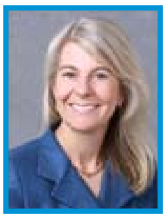
Sylvester explains that pre-crisis, securities lending in the US became a business with a significant focus on generating yield in reinvestment pools as opposed to exclusively on the intrinsic value of the loan itself – something that she notes is a reversing trend.

"Getting back to basics, really focusing on the value of the loan itself and not deriving the majority of the yield from the reinvestment is a very healthy return to a more sensible business practice," she notes.

Sec lending demand

Still, Judy Polzer, global head of securities lending product based in New York, is concerned about the potential for indirect impact of the combination of regulations on the demand side of business.

"The changes you are seeing in securities lending over the last couple of years are really being driven by the demand side as brokers de-lever and take risk off. Many of them are focused on capital and balance sheets to a greater degree – the question becomes, are they going to have an appetite for securities?" Polzer says.



Collateral is the centre of all of the reform requirements

Anne Sylvester

Americas head of client management and technical sales, Financing and Market Products

In general, the securities lending market has emerged from relative obscurity to become better understood as a liquidity mechanism. But the Lehman crash hangover and accompanying stigma from cash reinvestment portfolios going bad continues.

Meanwhile, the regulations keep piling on. Dodd Frank alone started with some 300 to 400 rules across a dozen agencies and there are still scores yet to be written. It is hard to tell, explains Polzer, how rules written and yet to emerge will affect the industry. This includes

Dodd Frank, Basel III, Solvency II, short selling rules from the European Commission and a myriad of other regulations such as those from Germany and the UK.

At the time of writing, infighting among five separate agencies working on the Volcker Rule has been reported by the New York Times.

Even before any mandated regulatory compliance, however, Polzer has identified an inherent duration mismatch. Brokers are looking to put on term trades but some lenders are more comfortable with shorter durations and the market is still working through this.

CCPs coming up on the derivatives side may create an increased demand for treasuries

Judy Polzer
Global head of securities lending product

Notably, the equity markets continue to show stable balances as the business is more a value than volume proposition, says Polzer, though short selling rules and tax harmonisation requires constant monitoring. Despite market jitters and massive volatility over the summer months, equities are doing okay.

The big story is in the fixed income space, where changes are taking place amid competing forces.

"It is a little bit too interesting a time to be in sec lending, we will have to see how it all plays out," Polzer says, "CCPs coming up on the derivatives side may create an increased demand for treasuries depending on how much they are trading, meanwhile there is a glut of treasuries in the market place with very little spread between different asset classes and agencies, for example many US FI non-cash trades are at very low rates."

That means collateral, particularly high grade government debt, may become expensive and in-demand and, as a consequence, more attractive and tempting to lend.

The preliminary numbers circulating peg the overall amount of extra collateral required at some $2 trillion dollars while the buy-side view via the Investment Management Association (IMA) in the UK cites an average initial margin requirement for its member firms in the region of 10 per cent of nominal value (based on prevailing OTC derivatives exposures), according to a whitepaper by risk management consultants, Intedelta.

Whether or not these figures are accurate remains to be seen, but one thing is for sure, the amount will be large.

The resulting dynamics have important implications because, as Anne Sylvester had noted, one of the obvious ways of getting the inventory is by trading up collateral via securities lending.

Collateral upgrade

Globally, collateral upgrade trading is an opportunity for the industry and potentially a strong demand driver, says John Rivett, who works with Sylvester as global business executive for collateral management, based in London. He oversees the core collateral management product suite and believes that as a collateral manager, OTC clearer, securities lender and equity and fixed income repo house, WSS is well-positioned to service the anticipated demand.

"[Market participants] are going to have to get the right type of collateral to be able to post into CCPs or independent margin accounts. As a tri-party collateral manager for stock lending and equity repo, both equity and fixed income, we have multiple solutions to offer," he says.

Collateral can be upgraded through the J.P. Morgan stock lending desk, but clients can also access hundreds of lenders for this trade through tri-party. That gives the broadest range of options, he notes.

"If you look at any economic rationale, you are going to see costs have to rise, since demand is going to be significant. Ultimately this is good for securities lending and will bring spread into the market. The CCP is going to set its rules and needs to post eligible collateral. The common view today is that supply may be limited, and with limited supply and huge demand, prices will rise and hopefully bring more supply into the market," Rivett says.

Once gold is held in J.P. Morgan's London account, it is a dematerialised asset that can be moved back and forth

John Rivett
Global business executive for collateral management

As a collateral manager, J.P. Morgan is top of the list when it comes to securities lending and as some of the regulatory uncertainties dissipate, Rivett points out that investment in technology and human resources being made now will allow the firm to help clients get the most out of their balance sheets.

"For all the volatility in the market, we are seeing relatively stable equity balances at the moment and new clients are coming on at a faster pace than have for many years. Optimising the balance sheet is going to be absolutely fundamental and effective collateral management is the best way of achieving that. Clients are looking for that efficiency, especially as there are many challenges in the marketplace," he adds.

And, as clients seek that optimisation, they can now use their gold holdings as collateral within J.P. Morgan tri-party. With the CME and LCH. Clearnet accepting gold as collateral and Swiss Securities Services settling gold as a currency, J.P. Morgan has launched its own initiative to make the most of the yellow metal through the unallocated London gold market.

"Gold is just another asset, says Rivett. "From a collateral management perspective, it is operationally akin to a treasury, a corporate bond, an equity or an ADR. As collateral agent, we manage the book entry movement. Once gold is held in J.P. Morgan's London account, it is a dematerialised asset that can be moved back and forth.

"Gold in the London unallocated market is relatively straightforward; it is how the markets operated for a very long time. We are quite pleased we have been able to leverage gold as a collateral asset by linking two J.P. Morgan businesses. Clients are looking at all the inventory on their balance sheet and where they can place all of their assets. Although gold is a very high quality asset, it has historically been viewed as relatively immobile. When you are looking at financing and funding, you want to be able to mobilise all of your assets. Being able to use gold as part of your collateral mix is a definite advantage," he says.

European risks

Despite the opportunities, like most market participants across the industry, J.P. Morgan's representatives at the conference are carefully monitoring individual market risk in Europe. In the time it took for the RMA event to wrap-up, Slovakia's government disintegrated after rejecting a call to expand the EFSF, the parliament agreed to an early election and completed the eurozone ratification process.

In addition to bolstering the EFSF, European leaders and central bankers remain under intense pressure to roll-out a comprehensive plan to recapitalise the region's banks and resolve the Greek sovereign debt crisis and contagion fears.

If there is a message from the RMA conference with regards to Europe, where market uncertainty is particularly unsettling as the region is a major economic force, it is that the industry is living up to the stress of ensuring systems and processes manage risks tightly while also preparing for global regulatory reforms to roll-out.. **SLT**

Indonesia

Indonesia is continuing its march towards becoming a global economic power

ANNA REITMAN REPORTS

While slowing growth in Asia hits the headlines, some commentators are pointing to bright spots such as Indonesia, where strong fundamentals are prompting economists to forecast a robust economy for the long-term.

In October, the Bank of Indonesia (BI) unexpectedly cut interest rates 0.25 basis points to 6.5 per cent, as the country's central bank turns more upbeat about the outlook for inflation.

So far this year, Indonesia's CPI headline inflation rate has been trending downwards and fell to 4.6 per cent in September compared to the same month in 2010. BI expects inflation to be below five per cent at the end of this year and sees it even lower in 2012.

In a recent report, Standard Chartered notes that Indonesia is set to become one of the world's fastest growing economies – with full potential of eight to nine per cent from a current 6.5 per cent annual growth in GDP - in part due to a rising middle class and urbanisation.

"We expect Indonesia to enter the club of world's largest economies in 2020 and the top six in 2030," write Standard Chartered analysts.

In particular, the bank notes that Indonesia's large domestic market cushions the economy from external shocks and fosters the development of banks, non-bank financial institutions and financial markets.

Indonesia is the world's largest archipelago, covering over thousands of islands and kilometres along the equator, throwing up challenges in the development of infrastructure to knit the country together, a crucial factor if the "demographic dividend" is to be exploited. The country has one of the world's youngest populations, with 60 per cent of the population below 30 years of age dominated by a higher concentration of early-age working population.

But the country must overcome various challenges such as bureaucratic inefficiencies and corruption, income and social inequality and, in part because growth opportunities are in the commodities and mining sector, environmental degradation.

At the same time, the financial services industry is expected to become an important beneficiary of growth dynamics and pressing infrastructure needs, and credit penetration is currently low, with a credit to GDP ratio of 32 per cent, compared with 70 per cent in Thailand and 90 per cent in Malaysia.

"We expect consumers and SMEs to be the key drivers of loan growth in the years ahead. We also see considerable growth potential for non-bank financial institutions such as insurers, mutual funds and finance companies. Rising incomes will encourage consumers to seek insurance and investment products in the form of mutual funds. The rise of the middle class will also boost demand for pension products; at the same time, Indonesia's demographics are likely to remain highly favourable over the next two decades."

Banking sagas

During the global financial crisis, the bailout of a small commercial bank, Bank Century, exemplified the challenges BI faces when its decisions are exposed to political processes.

The contested 2010 rescue plan devolved into bitter divisions over the fate of pro-market policymakers at the cabinet level, who also faced criminal investigations as a result.

That may not bode well for other complicated political processes that are sure to dramatically alter the banking sector and capital markets, chiefly the planned creation of a new regulatory body, the Otoritas Jasa Keuangan (OJK), based on the British Financial Services Authority (FSA) – legally scheduled for creation last year.

The BI law of 2004 requires the central bank to eventually relinquish its banking regulatory powers to the OJK, which will also incorporate BAPEPAM, the current capital markets regulator. But deadlock between BI, the parliament and the Ministry of Finance (MoF) has delayed the process.

BAPEPAM regulates the securities industry, while the MoF regulates insurers, finance companies and pension funds. However, should the OJK be created, the MoF could also hand over its regulatory responsibilities to the OJK, leaving the MoF primarily to manage fiscal policy.

"A key challenge for both BI and the MoF is the establishment of a crisis protocol that will provide a legal basis for BI, the MoF and the deposit insurance body (LPS) to bail out commercial banks in the next financial crisis, if needed. Without such a protocol backed by a law, regulators and policy makers could be reluctant to act rapidly contain even a minor liquidity crisis, which could spread to a full-blown banking crisis."

In 1998, the local currency, the rupiah, plummeted amid a strong demand for US dollars starting a familiar downward spiral: nervous lenders refused to refinance maturing loans, investors cut down and then reversed funds flow, borrowers chased dollars followed closely by investors and several banks ran out of dollar notes. A difficult period of transition in the country followed the crisis. Standard Chartered, however, thinks another 1998 banking crisis is unlikely.

Equity markets

Using market capitalisation as a best measure of the development of equity markets across countries, Indonesia's equity market has been one of the fastest growing among other significant economies, at compound annual growth rate (CAGR) of 30 per cent, during the last six years, though it is still notably small at 50 per cent of GDP in 2010, wrote Standard Chartered.

"Between 2008 and 2010, stock-market capitalisation growth has been led by the manufacturing, consumer-goods, and finance sectors. In contrast, the market share of infrastructure stocks has continued to decline, indicating slower growth than the market aggregate. The combined share of basic industry, property and agriculture stocks has remained small, at less than 15 per cent."

It expects continuing growth in market capitalisation to be driven by three structural forces: corporates' need for capital to fund growth, a move from labour intensive to capital intensive activities as well as a shift from primarily domestic operators into globally competitive players.

This should increase financing demand across sectors, but especially from high-value manufacturing, consumer-goods, and possibly mining and agriculture companies.

Indonesia has a low level of household and corporate leverage; going forward, banks and NBFIs will need to significantly increase their capital to meet financing demand, and this would typically be done via the debt and equity markets.

"Economic development often goes in tandem with economic reforms, including the privatisation of state-owned enterprises (SOEs)…Unfavourable market conditions and a failure to meet listing requirements are among the main impediments. The Ministry of State-owned Enterprises said in March 2011 that SOEs' market capitalisation represented only about four per cent of total market capitalisation, compared to their potential to reach a 25 per cent share. As the economy expands, we expect initial and secondary offerings for SOEs to pick up in the years to come."

Banks and NBFIs

Financial intermediation in Indonesia is low compared to other emerging-market economies, still, Standard Chartered expects significant long-term loan growth potential for the banking sector driven by small and medium sized enterprise and consumer loan growth but also potentially investment related spending, particularly for infrastructure projects.

Meanwhile, non-bank financial institutions (NBFIs) are gradually playing a more important role in Indonesia's economy, which the MoF classifies as insurance funds, finance institutions and pension funds, instead labelling mutual funds as an asset class.

In its assessment of NBFIs, Standard Chartered notes that assets grew at a CAGR of 21 per cent between 2005 and 2010, while mutual funds recorded a CAGR of 39 per cent and total assets more than doubled in size during the same time frame. "Considering Indonesia's population growth and rapid economic development, we expect robust growth in NBFIs to last another

10 to 20 years," notes Standard Chartered.

Insurance is one of the most developed NBFI sectors with growth driven by two independent segments: the government social security programme and private life insurance.

In 2010, the five social and public state-owned insurance funds made up 42 per cent of Indonesia's total insurance assets in 2010; they are non-competitive, invest in fixed income, and are growing steadily on the back of compulsory annual contributions.

Sec lending market

There is an OTC securities lending market in Indonesia, however, it is unclear what the size and scope of this market is. Brokers can enter into bilateral arrangements with approval from the BAPEPAM as long as they use a standardised agreement.

That is where Indonesian Clearing and Guarantee Corporation (KPEI) comes in. Operating since 2002 and trading since 2004, KPEI received a push as a result of regulatory mandates towards market development for growth and infrastructure.

As the CCP, it provides centralised services through electronic clearing (e-clear) as well as the standardised agreement to borrowers and lenders, which are also members of the clearing facility. Currently, there are 117 clearing members, of which 98 brokers and three custodian banks are participants in the SBL market.

At the moment, it has 118 stocks eligible for SBL from approximately 416 listed stocks on Indonesia's capital markets, though every month the list is adjusted. Of eligible stocks, 23 are SOEs and 44 stocks are available for short selling.

"We try to eliminate systemic risk in collateral management. The transfer of the collateral is through the CCP…and we guarantee the settlement," says Hoesen, president and director of KPEI.

Custodians are restricted from being borrowers but have been accepted as lenders to compensate for the fact that insurance, pension and mutual funds are barred from participating in equities-related SBL activities. Moreover, it is primarily a local broker lending to foreign broker borrowing market. Year-to-date, KPEI has seen over 1,450 transactions compared to roughly the same for all of 2010.

Transaction volumes are at some 560 million with a value at around $165 million.

Notably, there are no margin requirements for transactions, instead, the risk management model is integrated between the SBL side and the Indonesian Stock Exchange (IDX) with pooling of collateral. All SBL transactions are collateralised and as a result, transactions are subject to both the size of the lendable pool and the availability of collateral.

Hoesen explains that the system is designed such that any failure to return securities to the lender once they are recalled results in a payment of 125 per cent of the highest price on maturity date to the lender, guaranteed by KPEI through an alternate cash settlement.

At the same time, brokers can borrow securities directly from KPEI to avoid fails but must have an SBL contract to avoid the expensive penalty.

Looking to the future, KPEI's development plan aims to create supply and demand in the market as the clearer conducts workshops and engages in discussions with regulators and relevant associations on initiatives.

"One initiative is to improve the ETF and derivative markets, so we can provide securities financing through the SBL. We are also looking to include the insurance, mutual and pension funds industries, but at the moment establishing the OJK is the priority for Indonesian regulators. Another initiative is to expand membership to custodians as general clearing members," Hoesen says, adding that workshops and discussions with BAPEPAM and relevant associations are ongoing.

That multi-tier model of both individual and general clearing members comes from LCH.Clearnet, he explains, while to develop a bilateral scheme for the SBL market, KPEI is looking to the Korean model.

Custodians familiar with the market define the available securities lending activities as "fails related to support custody services". Though there are plans to expand the role of custodians to become borrowers, for now they behave as settlement agents receiving instruction to transfer shares to KPEI.

DBS Bank (Indonesia) has made the service available to clients for almost a year, but the response has been below expectations.

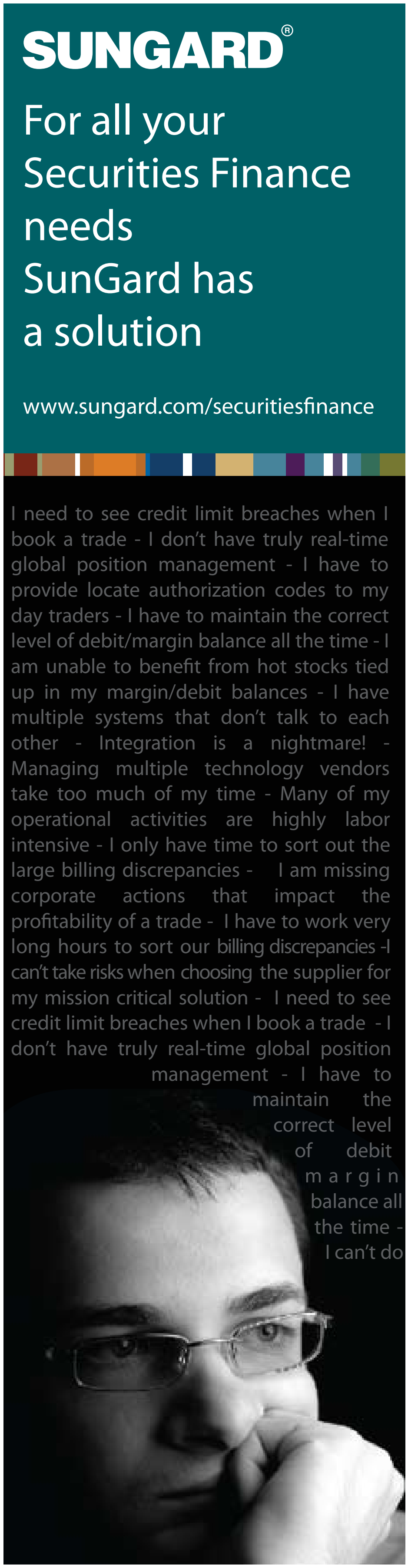
Endang Triningsih, vice president of Securities Services at DBS, says that client are unsure of KPEI's role in the market and express concerns over the level of counterparty risk they are exposed to as well as question procedures around timely replacement of shares out on loan.

Triningsih was involved with KSEI, Indonesia's central securities depository, for seven years prior to joining DBS and participated in the development and implementation of scripless trading and book entry settlement. At that time, she introduced KSEI developments to local and foreign markets.

DBS clients that could benefit from SBL are generally local fund managers she explains. Since pension and insurance funds can only invest in government and corporate bonds by regulation, investment potential is limited.

Still, she notes that the commission is "very attractive". KPEI charges 15 per cent to the borrower and provides 12 per cent as the commission to the lender. Domestic clients are subjected to a withholding tax rate of 15 per cent and offshore clients are subjected to a withholding tax rate of 20 per cent or other applicable treaty rate.

But to attract clients, more needs to be done she says. "KPEI, as the self regulatory organisation (SRO) and central counterparty, needs to do more education about their role and function in the Indonesian stock market and its development to foreign investors" Triningshih says, "The investors, local or foreign, may understand that actually, SBL could be an investment alternative instead of a settlement risk solution only." **SLT**



Under the hammer

SLT speaks to eSecLending's Chris Poikonen about the company's development of securities lending auctions

ANNA REITMAN REPORTS

SLT: Could you explain where eSecLending fits into the securities lending market?

Chris Poikonen: eSecLending is a full-service global securities lending agent providing customised securities lending solutions for institutional investors worldwide. We are the only independent agent in the market and one of the largest third party providers. Our philosophy applies investment management practices to the securities lending industry. Our differentiated process utilises a transparent, disciplined and repeatable auction process to determine our clients' optimal lending strategy and facilitate best execution. Our performance is driven by innovation and validated by client satisfaction and industry recognition. Our people are committed to delivering thoughtful solutions and developing long standing partnership with clients.

With over ten years of experience we are active in 33 markets and have over 100 employees dedicated to securities lending who are located in our offices in the US, Europe and Asia.

eSecLending pioneered the use of auctions in securities lending. Having auctioned over $2 trillion in assets for beneficial owners since inception, we have more experience than any other provider in the industry in structuring optimal securities lending programmes utilising a disciplined and transparent process. We believe in the auction process. We have spent years perfecting the model and investing the knowledge and capital necessary to improve the process. We put our clients' interests first and do not try to be all things to all lenders.

SLT: What was the impetus for development of the auction process?

Poikonen: eSecLending was founded in 2000 to provide an alternative approach to securities lending for institutional investors in an effort to address what we saw as the limitations of traditional custodial and other third party pooled lending programmes. Our origins began in the late 1990s as part of an asset management firm where we were looking to establish a securities lending programme for portfolios managed by United Asset Management / Old Mutual. During our review process, we determined that securities lending should be treated as an investment management and trading discipline rather than an operational function.

We observed that many concepts that had been employed for years in the investment management industry were largely absent in the securities lending market. Concepts including best execution, multiple managers, best-in-class specialist providers, competition among managers, performance measurement and benchmarking were not widely incorporated into the securities lending market. As a result, we developed a different approach by developing an auction process to optimise client returns and justify their mandate allocations.

SLT: How does this process address the concerns of beneficial owners?

Poikonen: A disciplined, transparent and repeatable auction process is a powerful tool for optimising your lending programme. Auctions are not a "route to market", rather they facilitate informed decision making as to whether assets are best suited for exclusives or discretionary lending (As an agent, we are unbiased as to which route the lender takes). The auction allows for full customisation and there are varying structures available that can accommodate common beneficial owner objectives. One misperception in the market is that auctions are complex and require more resources from the beneficial owner however the time and effort required to conduct an auction is not dissimilar from beginning any new lending program.

The industry evolution has made auctions more relevant than ever before and we are seeing increased demand for information. Auctions in the securities lending industry enable beneficial owners to achieve maximum price discovery by capturing the inefficiencies of the lending marketplace for the benefit of the lender. In addition, an auction is well positioned to respond to lenders' increased focus on optimising intrinsic returns as it secures the premium returns that borrowers are willing to pay for exclusive access to the lending value of attractive supply. Based on the results of an auction and in conjunction with the guidance of an agent, lenders can make informed lending decisions/allocations based on actual market data.

SLT: How does the auction process work?

Poikonen: While the process is quite simple, it is important to note that not all agent auctions are the same; look for a disciplined and repeatable process. In eSecLending's model, we typically auction assets first to determine the optimal route to market (ie, agency exclusive or discretionary) on each portfolio or subset of portfolios. In both programmes, our philosophy is to allocate to the best bidder given each client's guidelines and risk parameters. Our auction model enables clients to benchmark their returns and measure their performance against the market for their given assets, parameters, guidelines and risk tolerances. Using a market based approach is truly unique in the securities lending industry and we are the only lending agent that uses the auction as a means to assess demand before allocating assets to agency exclusive or traditional agency routes to market.

Many of our clients use our auction as an annual optimisation tool to allocate between our programme and potentially other relationships if deemed advantageous to them. Some view our process as a form of an "annual RFP" that provides the proof to boards, management and auditors that the firm is achieving best execution for their beneficiaries.

SLT: How was your presentation received at the IMN European Beneficial Owners conference in September? What were some of the issues raised?

Poikonen: The workshop was well attended by a diversified set of beneficial owners of all sizes. People were most interested in learning about the "auction process" and how it can be utilised for both outperformance and risk mitigation. The majority of attendees want their securities lending programme to be a customised offering built around their unique requirements. An off the shelf securities lending product designed for the masses is no longer acceptable in this environment.

SLT: Are there any geographical factors in play in the level of interest for the auction process?

Poikonen: No. The eSecLending Auction Process can translate across markets as the process is increasingly proving to be a valuable price discovery tool used to facilitate informed decision making.

SLT: What are some of the challenges and opportunities in the current securities lending market place for new ideas like this?

Poikonen: Although securities lending auctions are not new, they are certainly being viewed with a fresh perspective given their increasing relevance in today's market.

Launching new innovations in today's market can be challenging for institutions that are tightly managing costs or are subject to the objectives and priorities of their other/primary business lines. Firms who can continue to innovate and refine their products during periods of volatility will be well positioned to respond as beneficial owners evaluate alternative providers. **SLT**

Long OYO, short IO's IOUs

SunGard's Andrew Shinn looks at the seismic technology sector to see how short selling data helps firms make a long/short trade

MARKET PERSPECTIVE

In the energy sector, seismic technology firms play an important part in helping exploration and production (E&P) companies locate oil and gas and then efficiently extract the deposits out of the ground. The process of mapping the sub-surface of the earth starts with a burst of energy, either from a giant vibreosis truck or a blast of dynamite; to map the ground below the oceans, air guns are fired from ships. The sound that bounces back from the ground or the ocean floor allows seismic firms to build 3-D models of the Earth's crust. In fact, many firms offer 4-D models, with time being the fourth element, that show how oil and gas deposits are moving through the earth during excavation.

The main revenue source for seismic firms such as OYO Geospace (NASDAQ:OYOG) and Ion Geophysical (NYSE:IO) is capital expenditures from E&P companies, which are driven by higher projected long-term oil and gas prices. While the price of natural gas is still depressed because of excess supply, the stable price of oil has allowed oil majors and E&P companies to increase their capital expenditure budgets. In fact, investment bank Dahlman Rose & Co. has predicted that 2011 exploration spending will increase 14 per cent globally and 22 per cent in the US, and both OYO and Ion should benefit. But there is a major difference between the two companies: OYO has remained profitable over the past few years, despite the downturn, while Ion has continued to struggle due in part to a number of failed acquisitions.

In addition to seismic data acquisition equipment, OYO manufactures communication transmission cables, armoured cables built to stand up to the harshest marine conditions, earthquake detection devices, and thermal imaging printers. Over the past three years, OYO has devoted seven per cent of revenues, or $9 million annually to research and development. This has helped the company continually expand the scope of its product market.

Innovation is crucial in seismic technology because advances in seismic data acquisition help E&P companies reduce the time and cost of going from drilling the first hole to starting production. For example, wireless stations can be more easily deployed in inhospitable landscapes. In 2008, OYO developed land-based wireless data acquisition stations, and the following year the company introduced a wireless version for marine-based data acquisition. In addition, OYO has a patented process for marine-based data acquisition that is still wired. To recover disconnected data stations, it utilises an air bag that automatically inflates when lines are severed; this is a huge advantage for OYO, and it is its most valuable patent (it expires in 2013).

While OYO has generated $14 million, $1 million, and $14 million in annual profit over the last three years and a three-year average return on capital of 11.9 per cent compared to a cost of capital of 8.1 per cent, Ion has lost hundreds of millions of dollars over the same time period. Its net losses between 2008-2010 were $38 million, $113 million, and $293 million, respectively. Its three-year average return on capital is 0.7 per cent compared to a cost of capital of 7.5 per cent. As a result, Ion has cut back on research and development, from seven per cent of revenues (or $50 million) from 2007-2009 to five per cent of revenues (or $25 million) in 2010. The decline in research spending is likely to hurt Ion's competitiveness going forward.

Ion's problems appear to stem from its failed acquisitions. In 2008, Ion recorded a goodwill impairment charge of $155 million, fully impairing the goodwill in its land-based business. The same year Ion also took an $87 million impairment of goodwill in 2008 related to a prior acquisition in its Solutions unit.

In 2010, Ion spun off its land-based business by establishing INOVA, a joint venture with China National Petroleum Corporation (CNPC), the largest integrated oil and gas company in China. Ion retained a 49 per cent ownership interest in the venture, and it continues to take losses on it. In 2010, Ion recorded a loss of $38 million on the spin-out restructuring and an additional operating loss of $24 million the same year. Revenues from INOVA have decreased from $144 million in 2008 to $16 million in 2010.

Despite the losses, Ion continues to operate in part by issuing new shares of stock. The number of shares outstanding increased from 79 million in 2006 to 144 million in 2010. In 2010, 23.7 million shares of stock were sold to CNPC for $2.80 per share, a 42 per cent discount from Ion's share price at that time. What may concern Ion shareholders is that "the terms of China National Petroleum Corporation's investment in Ion contain a number of restrictive provisions… [that] may adversely affect Ion's ability to quickly raise funds through a future issuance of securities." In addition, "liquidation of INOVA or China National Petroleum Corporation would constitute additional events of default under the Credit Facility."

While it's unlikely that the Chinese government would not backstop CNPC, the future of INOVA, a small joint venture that is currently losing millions of dollars per year, is less certain. And without being able to generate cash as easily by issuing debt or equity in the future, Ion loses flexibility to fund its ongoing operations. Furthermore, seeds of doubt regarding revenue recognition at what is now INOVA were planted in 2009 when Ion announced that it discovered a "material weakness in internal controls over financial reporting" in Ion's land-based business, specifically "an error in revenue recognition." As a result, Ion restated its unaudited consolidated financial statements in 2009.

Investors may decide to go long OYO and short Ion. This would hedge against a potential continued decline in the industry, but if E&P expenditures increase and seismic firms profit, the trade would take advantage of OYO's superior position compared to Ion. Short sellers of Ion would not have to pay much to borrow shares of Ion because borrowing costs are currently seven bps. Nevertheless, it would be helpful to monitor SunGard's Lending Pit system going forward to protect against potential short squeezes. **SLT**

Andrew Shinn
Vice president, sales and development
SunGard Astec Analytics

Training and Education

Open Courses	**London** **New York** **Singapore** **Sydney**	**Hedge Funds: A Credit Perspective** A two-day intensive workshop offering an in depth structured approach to the analysis of hedge funds and alternative investment strategies. The workshop takes a credit focus for bankers and analysts but is also appropriate for a wider audience who need to understand the key risk issues of the hedge fund industry.	**Fitch Training**
Open Courses	**Frankfurt** **Hong Kong** **London** **New York**	**Basel II & III: Bank Capital Adequacy** A two day case study based workshop for financial market professionals, focusing on the capital raising, funding, investment and risk management needs of banks in the context of changing markets, Basel III and other regulations.	**Fitch Training**
26-27 Oct	**London**	**The Repo Market** The repo market is the lubricant that keeps the financial engine running. It serves as the link between the money and capital markets, and is vital to the well functioning of the financial markets. The turmoil in the market over the past two-years has further enhanced the importance of the repo market.	**Eureka Financial**
9 Nov	**New York**	**Repurchase Agreements (Repos) and Securities Lending** By the end of the course participant will be able to: Describe the features and characteristics of secured financing: - Repo agreements - Securities lending programmes	**Financial Markets World**
9-10 Nov	**London**	**International Securities Settlements & Custodial Services** This training programme is designed to provide delegates with practical knowledge about the key concepts, systems, processes and procedures in international securities settlement and custodial services as well as operational risks involved. Participants will have a chance to gain skills necessary to facilitate day-to-day transactions and communication processes between all parties involved	**Eureka Financial**
16–17 Nov	**London**	**Collateral Management** This course looks at collateral management in OTC derivatives in particular as well as repos and securities lending and borrowing. Risk identification, control, documentation, types of collateral, gross and net exposure and other practical aspects are covered as well as the conceptual framework and practical problems egg the treatment of corporate actions on a borrowed/lent position.	**Investment Education PLC**
23-25 Nov	**London**	**Global Master Agreements for Repo and Securities Lending Workshop** The International Capital Market Association (ICMA) and the International Securities Lending Association (ISLA) will be holding a workshop on the Global Master Repurchase Agreement (GMRA) and the Global Master Securities Lending Agreement (GMSLA).	**ICMA and ISLA**

Industry appointments

HazelTree Fund Services has appointed **Wilson Pringle** as a managing director in its New York office.

Prior to joining HazelTree, Pringle was co-head of business development for Stanfield Global Strategies' financing businesses with over $25 billion in assets and Head of North American Client Services covering hedge funds and asset managers for JP Morgan's Global Derivatives Services Group.

At J.P. Morgan his team was responsible for delivering valuations and operational support for equity, credit, interest rate, and Fx OTC instruments. Wilson also served as senior consultant for IBM's Banking, Finance, and Securities practice and began his career at Morgan Stanley in Fixed Income trading.

Netik has started a major investment push in the Delta One space with the recruitment of a new team to its Delta One index and ETF data division. The Delta One team spans technology, product management and sales across Netik's three key regional centres of New York, London and recently opened Hong Kong.

Netik acquired Capco Reference Data Services in 2008, formerly known as Iverson, which was founded in 1983 and have been providing index and ETF data for over 10 years. Netik has a strong track record in the Delta One data space and were the first to deliver Delta One Data as a service - quality, timely and accurate global index and ETF data across all asset classes in a single format, validated and customized 24 hours a day.

Bernie Thurston joins to lead the Delta One data business, together with **Giles Sarton** who heads up global Delta One sales, bringing with them two decades of expertise in the index and ETF space from Markit Equities division. Both will be based out of Netik's London office.

Joining Thurston and Sarton in London are **Femi Orangun** and **Mark Frost**, both of whom have joined the Delta One technology team, focused on the development of the platform, tools and database. Orangun spent over six years architecting and implementing solutions for the index and ETF data aggregation platform at Markit and Frost brings with him 15 years of banking IT experience from Goldman Sachs including infrastructure, front and back office roles.

In New York, **Paul Tompkins** joins Netik to lead the Delta One technology team bringing his experience of building Delta One trading applications from Deutsche Bank and Macquarie.

In addition, **Brad Diamond** also joins the New York office, to focus on Americas Delta One sales, reporting to Sarton. Prior to joining Netik, Diamond was senior sales director for 12 years with Standard & Poor's.

Netik sees Delta One Data as a key growth area in the marketplace. Thurston, Head of Delta One, commented, "We are seeing an increasing trend as the market looks for alternatives to the traditional equities to increase overall profitability." Increasingly, investment banks are looking to the creation and management of synthetic ETFs as the way to achieve sustainable revenue, with Europe now following fast in the footsteps of the US, which has been more aggressive in the Delta One space. Thurston continued "Netik uniquely brings together data and tools meaning we are ideally positioned to embrace the growth opportunities and requirements for Delta One globally."

Rob Flatley, CEO, Netik, commented, "The new team will focus on bringing together data and technology in the creation of new and innovative solutions for the marketplace. Delta One Data is a key part of our growth plans and the tremendous level of experience and skills that Bernie and his team bring to Netik will ensure that Netik maintains and expands its presence in the Delta One space."

eClerx has announced the appointment of **Artie Schlesinger** as senior manager for its hedge funds and prime brokerage business. In this role, Schlesinger will be focused on providing support and guidance to clients in the hedge fund and prime broker space.

He has more than 20 years' experience in the financial services industry and joins eClerx from Caxton Associates, where he was the global head of operations.

BNY Mellon has appointed **Jim McEleney** as chief operating officer for Europe, Middle East & Africa, based in London.

McEleney was formerly CEO of BNY Mellon's operations in Pune India and a member of the company's Asia Pacific Operating Committee.

As COO of EMEA, McEleney oversees the regional governance framework on behalf of all BNY Mellon businesses and operations in EMEA, and has full responsibility for the management of BNY Mellon's relationships with EMEA regulators.

Michael Cole-Fontayn, chairman of EMEA at BNY Mellon, said: "Jim is a strong and experienced leader with a deep knowledge of our business, both here in EMEA and globally. Over the past few years he has been instrumental in growing our operation in Pune, one of our global centres of excellence, and I have no doubt he will bring the same expertise, dynamism and commitment to his new role."

McEleney joined BNY Mellon via The Boston Company as a financial analyst in 1987. Having worked for many years in a range of US-based roles, McEleney relocated to London in 2006 to establish the first European office for BNY Mellon Wealth Management, serving the global ultra-high-net-worth market. Prior to joining Wealth Management, the majority of McEleney's career with BNY Mellon had been with asset servicing, where in his last assignment he served for three years as chief administrative officer of global asset servicing. **SLT**

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