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Facebook shares trigger restrictions on shorting

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Facebook shares prompted SEC rules on shorting after dropping by 13.7 percent in the opening minutes of trading on Monday 21 May.

Just 15 minutes into Monday's session, Nasdaq issued a warning stating that Facebook shares had triggered restrictions on shorting under SEC regulation SHO, after the stock dropped more than 10 percent from the prior day's closing price.

Shares of the much-anticipated IPO have fallen sharply since they opened at $42.05 on Friday 18 May amid an initial flurry of trading problems at the Nasdaq, and after news that top underwriters cut their revenue estimates just days before the offering.

After a $0.23 gain on Friday, the stock finished Monday down 11 percent and continued to slide on the morning of Tuesday 22 May.

Yet short sellers are still eager to bet against the stock given its lofty valuation.

Financial Industry Regulatory Authority daily reports on Regulation SHO trading reported that on Friday 23.6 million Facebook shares were sold short on the NYSE and Nasdaq combined. With the short sale restrictions in place on Monday, the number fell to 6.4 million.

Wednesday 23 May marked the first day that Facebook's securities were officially on loan, due to the three-day settlement rule for US securities. However, some managers began shorting the stock shortly after trading started on Friday 18 May.

"Facebook shares have had a much less volatile day on the lending markets", commented David Lewis, a senior vice president at SunGard. "Significant demand on Tuesday drove borrowing fees sky high driven by short sellers desire to be sure of their supply."

"Wednesday saw a flood of supply which, in line with simple supply and demand brought borrowing fees down by around 80 percent. Here they have stayed through

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NEWSINBRIEF

SunGard propels connectivity with Colombia

Bolsa de Valores de Colombia (BVC), the official Securities Exchange of Colombia, has certified SunGard as an international market data provider.

SunGard will source market data directly from the exchange and will distribute it globally via the SunGard Global Network (SGN), which provides multi-asset order-routing capabilities for institutional asset managers, hedge funds and broker dealers.

The addition of market data will complement SunGard's existing connectivity in Colombia: BVC certified the SunGard Valdi software platform for Exchange members to use on the BVC trading engine in November 2011.

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EquiLend lands Japanese trust bank

Securities finance trading and post-trade services provider EquiLend has signed up Japanese trust bank SuMi Trust (Sumitomo Mitsui) to its platform.

SuMi Trust went live on EquiLend's platform through its agent on 30 March. EquiLend expects several other domestic participants to join in the near future.

Brian Lamb, the CEO of EquiLend, said: "Having a bank of SuMi Trust's stature join the platform is a strong endorsement of EquiLend's suite of trading services and represents an important move for the business in the Japanese marketplace."

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Thursday, mimicking the share price which, at the time of writing, is flat to up a few cents. Recall volume has also been more subdued, suggesting that the rush to sell out has been stemmed, again, backed up by the relatively stable price."

The cost to borrow the stock varied from 5 percent to 50 percent on an annualised basis, according to securities lending sources; far greater than general collateral stocks, which lend at a few basis points, but below other recent Internet IPOs, such as those of Groupon or LinkedIn, which carried annual borrowing costs so severe that the bets against them were a few days at most.

Automated Equity Finance Markets, a securities lending agency in New York, said the cost to borrow Facebook stock on Wednesday was below a 10 percent annualised rate, for a theoretical cost of less than $3 to short a $30 stock for a year.

"We see 33 million Facebook shares out on loan," commented Will Duff Gordon of Data Explorers. "In absolute terms this is quite low, but represents 8 percent of the free float or 1.6 percent of the total shares outstanding (using Reuters shares outstanding numbers). This is based on trades settled on 23 May, and it's worth noting that shares are still being filtered into lending programmes, which of course is a necessary requirement before they can be borrowed."

"Given this limited supply, it is unlikely short sellers are responsible for all of the Facebook share price decline and it is worth remembering that demand to borrow shares following an IPO is often inflated by prime brokers' needs for market making purposes."

"Having said that, we see strong demand to borrow Facebook with 70 percent of the supply of available shares out on loan. However, the cost to borrow has fallen over the past day, from 10 to 6 on our score, with 10 being the most expensive and 1 being cheap, general collateral."

"The next junction for Facebook to pass is the commencement of options trading on the Chicago Board Options Exchange (CBOE) next week," stated Lewis. "Market makers will need to borrow and short Facebook shares in order to hedge the options that they write. The level of supply in the lending market will influence the shares borrowing costs and therefore impact the options prices; the harder to find the shares the richer the options price."

"Those investors wanting to take up bearish view will look hard at the implied volatility on different options contracts versus how expensive it is to borrow and short the shares, and then take up their positions."

"The CBOE usually waits longer after an IPO to begin trading options, and given the problems at Nasdaq on Friday, one would think that the CBOE would be extra cautious. An improvement in the ability to borrow shares in the securities lending market between now and then should ease some of those concerns and the need to obtain up to date data remains vital."

Battle for Asian prime brokerage

A survey by AsiaHedge has reported that Credit Suisse and Bank of America celebrated increased market share over 2012 in their Asian prime brokerage divisions, while Goldman Sachs and Morgan Stanley have lost hedge fund clients and assets.

Before 2008, the combined market share of Goldman Sachs and Morgan Stanley in the Asia-Pacific market was 60 percent. Four years later, their combined share dropped to 30 percent, with Credit Suisse, Deutsche Bank and UBS seizing more than 10 percent each.

The survey also revealed that the Bank of America flew past Citigroup in terms of number of assets, increasing assets by more than a third to approximately $6 billion.

However, assets under management for all players fell to $137 billion from $150 billion, as more than 80 hedge funds shut down.

SunGard propels connectivity with Colombia

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Maria-Jose Ramirez, the commercial vice president at Bolsa de Valores de Colombia, said: "BVC is a trading destination not only for trading participants in Latin America, but increasingly for European and American financial institutions."

Philippe Carré, the global head of connectivity of SunGard's capital markets business, said: "Access to Bolsa de Valores de Colombia's real-time data and brokerage trading connectivity through Exchange members can help SGN members increase their trading efficiencies and take advantage of the growth opportunities in this emerging market."

EquiLend lands Japanese trust bank

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"We currently work with a number of international trustee banks and custodians in the country. However, SuMi Trust represents a major pinnacle for EquiLend with the domestic Japanese trust banks."

Nobuyoshi Fujii, the senior manager of SuMi Trust's London branch, added: "SuMi Trust is a leading provider of one-stop global trust services including pension plan advisory, investment management and custody. With $770 billion AUM, our group is Japan's largest asset manager and one of the country's dominant custodians managing and administering significant public and corporate pension funds."

"We believe the integration of EquiLend's services into our securities lending operations will result in significantly improved efficiencies to the benefit of our customer base. Furthermore, the adoption of EquiLend will help improve the efficiency and liquidity of the Japanese equity market."

Clearstream and Iberclear to grow Spanish collateral management

Iberclear, the Spanish central securities depository and subsidiary of BME, and the international central securities depository Clearstream, have signed an agreement to develop a new triparty collateral management service for the Spanish market.

The service will target the collateralisation of exposures in the Spanish market of Iberclear clients.

In the first phase, it will cover the exposures resulting from domestic repo transactions, including the possibility of pledging received assets from a repo transaction with the Spanish central bank (Banco de España) in order to get access to central bank money.

The service will be launched ahead of regulatory changes that will require financial and non-financial institutions to improve their liquidity and collateral management efficiency. Through the Liquidity Hub GO (global outsourcing) service, it is hoped that Iberclear clients will be in a position to handle their domestic collateral holdings and exposures more efficiently, while keeping them in the domestic Spanish environment.

Jeffrey Tessler, the CEO of Clearstream, said: "It's a strategic priority of Deutsche Börse Group to make global markets more robust through risk and liquidity management solutions such as Clearstream's collateral management outsourcing service. Collateral has become a very scarce resource and sourcing good quality collateral is increasingly expensive."

José Massa, the chairman of Iberclear, said: "The service is a major step forward for Iberclear and

the Spanish market as it will allow our clients to manage their collateral holdings and exposure more efficiently without moving it out of Spain."

Iberclear will build on this initiative to broaden its range of custody services.

Clearstream's Liquidity Hub GO service went live with the Brazilian CSD Cetip in July 2011. Since then, further development plans have been announced between Clearstream and the Australian Securities Exchange (August 2011), the South African CSD Strate (January 2012) and the Canadian CSD CDS (March 2012).

The Accenture/Clearstream report, which is entitled Collateral Management: Unlocking the Potential in Collateral, was published in September 2011.

It revealed that the financial services sector could save more than €4 billion annually in collateral management costs by addressing operational inefficiencies.

Pershing offers new collateral management services

Pershing, a BNY Mellon company, has launched two new applications as part of the organisation's extensive enterprise collateral management offering that automates the process of moving collateral between the custodian and Pershing Prime Services.

The service is available through Pershing's NetX360, the company's technology platform for fund managers and investment professionals.

The two applications are called PrimeConnect and PrimeConnect40, the former providing transparency and control of collateral selection and movements to hedge fund managers using BNY Mellon to hold unencumbered assets, and the latter also offering transparency and online collateral movement to '40 Act fund managers using the tri-party structure to support alternative strategies.

"Increasing concern over counterparty risk, coupled with the traditionally cumbersome and time-consuming collateral management process, has led many fund managers to be cautious when pledging collateral to their counterparties," said Gerry Tamburro, the managing director at Pershing.

"PrimeConnect and PrimeConnect40 not only eliminate the phone calls, faxes and emails, but they provide a clear window into the movement and management of collateral. Because these applications provide both a consolidated view of an overall portfolio and an online and real-time margin calculator, fund managers are able to more efficiently and effectively place collateral."

Report outlines best practice for oversight

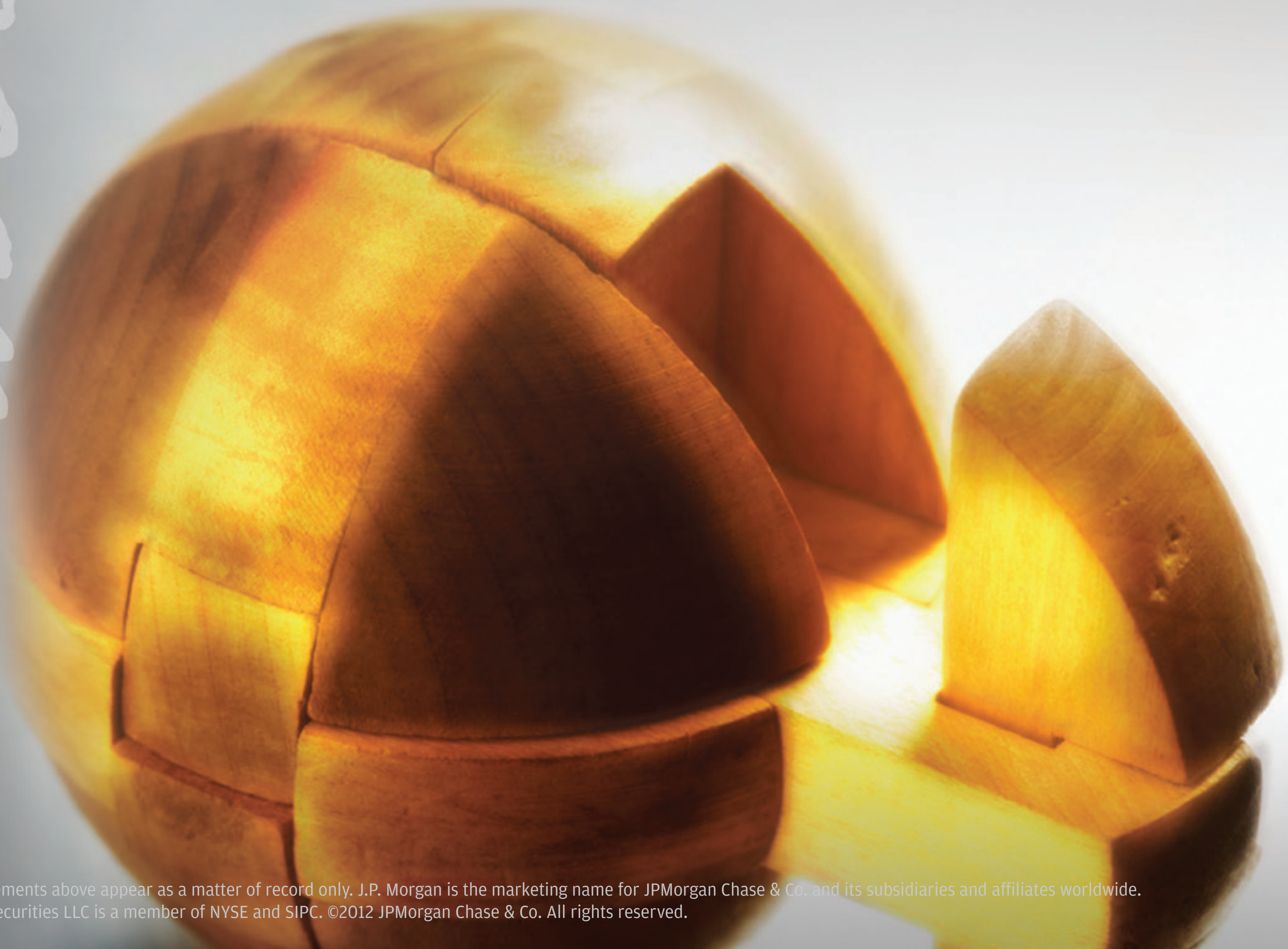
The Mutual Fund Directors Forum has released a special report entitled Practical Guidance for Directors on the Oversight of Securities Lending.

The report explains the ins and outs of securities lending, including risk management, to help directors make informed decisions about securities lending in their funds.

The paper is based on eSecLending's guidance paper that is aimed at those responsible for creating, monitoring and managing programmes in mutual fund and exchange-traded fund groups.

The company assembled a working group that was made up of professionals from across the securities lending industry so that it could develop an educational resource containing practical guidance for US mutual funds, according to eSecLending.

Working group participants included more than



30 representatives from mutual fund companies and related firms and associations. This effort led to a document outlining securities lending best practices.

Its document identifies sound securities lending practices, enhances understanding of the product and highlights issues and concerns that arise when starting, monitoring or changing a lending programme.

Of the Mutual Fund Directors Forum's paper, David Smith, who is its executive vice president, said: "In the wake of the market difficulties over the past several years, we've heard from members concerned about securities lending programmes."

"With this report, our goal is to provide helpful information that may assist directors in determining how to oversee securities lending activities and in deciding what questions to ask the adviser, their portfolio managers and others involved in the process."

"Securities lending plays a significant role in today's capital markets and is believed to improve overall market efficiency and liquidity," said Susan Ferris Wyderko, the president and CEO of the Forum, in a statement.

"In addition, securities lending plays a critical role in certain hedging strategies, acts as a useful tool in risk management and helps facilitate the timely settlement of securities trades. [W]e feel it's important that we arm our members with educational material on this topic to assist them in their important oversight work."

The Mutual Fund Directors Forum is a US-based organisation for independent directors of investment companies who are dedicated to improving mutual fund governance.

MXCorner

Opening up: transparent securities lending

Securities lending is often accused of being less than transparent, but is this fair and has there been any improvement over the last few years?

Regulators and commentators frequently describe our market as opaque, and to a degree, that is true. We are reluctant (perhaps understandably) to publicly disclose strategies, fee share, and even loan values, to the broader market. Consequently, market outsiders find information difficult to come by.

The industry has become more transparent to underlying schemes and investors that provide their assets for lending. In this space, there has been a significant improvement in reporting over the last few years and it is broadly recognised that investors are able to access information at a reasonably granular level, if required.

However, one issue that arises from this is interpretation. It may be easy to churn out transactional data, but analysing and understanding it takes a good understanding of market mechanics. Without this knowledge, it is easy for non-practitioners to come to unhelpful conclusions about the risks and rewards of the activity. Core lending systems often have reasonable reporting tools for transactional data, but it can be difficult to enrich this to make it meaningful within the system's limitations. Clients now want integrated risk modelling and capital calculations as part of their reporting package, as well as regulatory reporting requirements met on their behalf.

Regulators are beginning to push for increased transparency through various new regulations, including (but not limited to) liquidity reporting, Solvency II and short selling rules. These reporting requirements will involve a significant enrichment of transactional data to meet the prescriptive requirements being proposed. This includes investor protection through a full disclosure of the parameters and risk appetite before engagement, and an on-going reporting of risks and exposures.

There is little doubt that in the future virtually every aspect of this activity will need to be reported to regulators, and it remains to be seen how much of this information will then be made publically available. It seems that the industry remains at the other end of the spectrum to regulators in this respect, and engagement with regulators will be key to finding a happy medium.

When transparency is forced on the market, such as lending disclosures in Hong Kong, it seems to be able to react quickly to specific requirements, but solutions tend to be tactical and often manually created. How many tactical reporting solutions can a business take?

MX Consulting is working with clients to deliver strategic enriched data and analysis to meet existing and future reporting requirements on behalf of clients and regulators. Solvency II is one of the most challenging regulatory reporting requirements that the market faces and while this only affects insurance companies and some pension schemes at the moment, it is likely to affect a broader range of lenders over time and represents a huge challenge in itself.

One thing is for sure, while the industry has come a long way in terms of transparency, there is still more to do to meet future requirements. The ability to provide granular, enriched reporting and analysis, whether to clients, regulators or the rest of the market, will be a core factor in defining the future winners and losers in this market.

Sarah Nicholson, senior partner
MX Consulting Services

Emerging markets bank joins SunGard

Renaissance Capital, an emerging markets investment bank, has joined the SunGard Global Network (SGN) trading community.

Renaissance Capital will be able to provide brokerage services for the Russian markets to the more than 2,000 asset managers and 530 brokers linked by SunGard's international trading network.

SGN community members will also be able to route trade order flow directly to Russia's MICEX-RTS Exchange Group and the London Stock Exchange's International Order Book, where Russian stocks comprise 92 percent of trade volume.

Sam Atkins, the head of electronic trading group product development and exchange connectivity at Renaissance Capital, said: "Firms linked to the SunGard Global Network will be able to access our advisory services and leverage our expertise to access both emerging and frontier markets."

Philippe Carré, the global head of connectivity for SunGard's capital markets business, added that while investment firms and brokerages are looking to emerging markets for new growth opportunities, connectivity to the trading exchanges in these geographies is generally complex because of the lack of infrastructure and the need for local, specialist knowledge.

Calypso releases 13th update for OTC services

Calypso Technology has released Calypso V13, which is aimed at helping customers take advantage of opportunities created by the new OTC market structure in clearing and collateral management services.

Calypso V13 enables clearing member organisations to deploy in-house and client clearing services for interest rates/credit derivatives and FX products with initial/variable margin calculations across multiple clearinghouses, integrated collateral management, and treasury and liquidity services.

Kishore Bopardikar, the CEO and president of Calypso Technology, said: "We are helping capital markets firms address new front-office, operations and connectivity issues associated with the new OTC landscape, while managing margin compressions and capital costs across business lines."

According to TABB Group, nearly $2 trillion in additional collateral may need to be posted to com-

ply with proposed central clearing margin requirements, placing a strain on bank balance sheets.

"Centrally-cleared derivatives will turn the back-office from a cost centre to a critical tool for efficient allocation of capital," said Adam Sussman, a partner and research director at the TABB Group.

Deutsche Bank to open agency sec lending desk in Asia

Deutsche Bank is planning to open an agency securities lending desk in Hong Kong in the second quarter of 2012 so that it can provide a better service to its clients in local Asian markets.

Greg Chamberlain, who recently joined Deutsche Bank, will lead agency securities lending trading operations in Asia and will be based in Hong Kong. Chamberlain previously worked at Barclays Capital and has more than 20 years of experience in the securities lending industry.

Chamberlain will report to John Schreyer, the head of agency securities lending trading in EMEA and Asia at Deutsche Bank.

"Deutsche Bank is dedicated to meeting the needs of our clients in Asia, and the establishment of an agency securities lending unit in Hong Kong demonstrates our commitment to the business," said Mrugank Paranjape, the Asia head of direct securities services at Deutsche Bank. "This expansion of our footprint further strengthens our direct securities services franchise in Asia and enhances the value we bring to our clients."

Tim Smollen, the global head of agency securities lending at Deutsche Bank, added: "The Hong Kong desk will complete our agency securities lending coverage that is already in place in Frankfurt, London, New York, Poland and Turkey. We look forward to further supporting the agency securities lending needs of our clients by being in the same time zone, allowing us to best coordinate trading in local Asian markets."

"In addition, we are pleased to welcome Chamberlain, who will leverage more than 20 years of experience in the securities lending industry to help us increase our presence in Asia."

SunGard aids Japanese securities lending automation

SunGard has extended its suite of securities finance solutions with the launch of Apex JSFC Trade Manager, which helps to reduce the costs and increase the productivity of lenders participating in the Japan Securities Finance Corporation's (JSFC) daily auction of securities lending requirements.

Each day the JSFC publishes the borrow requirements of market participants so that holders of stocks can submit their best offers in an effort to capture those lending opportunities. However, many lenders rely on time consuming and error-prone manual processes to match each opportunity with available securities.

Apex JSFC Trade Manager automates the bid submission process, helping lenders save time, increase accuracy and reduce costs. Analytical tools help traders determine the best quantity and fee for each stock and make more accurate and timely bids.

Users can also take dividends into account and use decision support tools to help optimise their P&L in the auction process and facilitate funding/financing trades when they are looking to generate cash through the transaction.

Delivered on an ASP basis, Apex JSFC Trade Manager can be integrated with any stock borrowing and lending system for straight through processing, or it can be run as a standalone solution.

Jane Milner, the head of strategy for securities finance and enterprise collateral management for SunGard's capital markets business, said: "The Japan Securities Finance Corpora-

tion's daily stock lending process is a time-critical event that involves lending hundreds of stocks, analysing current positions and assigning fees. SunGard's Apex JSFC Trade Manager automates this process to help securities lenders capture the maximum revenue from Japanese lending opportunities and save time and costs."

Illinois pension fund adds Deutsche for sec lending

The State Universities Retirement System Board of Trustees (SURS) voted to retain Northern Trust as provider of custodial services for the organisation.

In addition, the board voted to hire Deutsche Bank to act as the system's securities lending agent. As directed by the board, SURS has chosen to implement a risk-averse strategy while continuing to maintain a lending programme.

Boom in brokerage for Mizuho

Japanese bank Mizuho has beat out analyst estimates to foretell 500 billion yen ($6.3 billion) in net income for the year ending March 2013.

In a statement to the Tokyo Stock Exchange, Mizuho said that net income would climb from the 484.5 billion yen that was recorded the year before, compared to the 378 billion yen average estimate compiled by Bloomberg.

The optimistic projection is a result of a leap in lending after an approximate two year slump, and the merging of two brokerage businesses. On 15 May, Mizuho Securities and Mizuho Investors Securities signed a merger agreement, and plan to conduct the merge on 4 January 2013.

The bank predicts profit from its brokerage business after a net loss of about 95 billion yen in the year ended March, chief executive officer Yasuhiro Sato said at a news conference in Tokyo.

However, a tumbling interest rate means that profit to be made on loans is not vast, and Mizuho still has the lowest net interest margin of Japan's three largest banks.

Staunton's View

No fate but what we regulate

If for a moment we could put aside our fears of economic turmoil within the eurozone, Greece's potential eurozone exit, austerity programmes and recession, we may rest a little easier at night. Unfortunately, we are indeed in very unstable times, and the powers that be are seeking to address instability with regulation.

The collapse of Lehman Brothers and the economic turmoil that ensued was the perfect catalyst for the huge wave of regulation that we now face. Politically, governments had to react to growing public discontent and had to be seen to be dealing with banks that were 'too big to fail'. Now we have to deal with the greatest level of regulation that we have ever faced.

The regulations that we have to deal with are:

- Dodd Frank

This was designed to promote stability, transparency and accountability. It was intended to put an end to the 'too big to fail' argument and to protect taxpayers who have funded bank bailouts.

- EU short selling regulations

The main goals of these are harmonisation, enhanced stability and greater transparency within the EU and its markets. The first draft was published (level 1 text) in March and the second level text is being discussed. This is an EU directive, which means that EU member states interpret the directive and implement it with their own national legislation according to predetermined timelines.

- ETFs, UCITS and the review of shadow banking

Draft ESMA guidance is aimed at increasing investor protection, standardising collateral policies and improving overall transparency for investors. Consultation on this closed in March 2012. There has been lots of progress and momentum, but no deadline for a final rule has been given.

The FSB (Financial Stability Board), which is made up of all of the members of the G20, is discussing shadow banking. The FSB has identified the need to strengthen regulation and supervision of the shadow banking sector due to concerns about migration of systemic risk from regulated markets. To be clear, 'shadow banking', which is a rather negative term, applies to financial firms that transact beyond any national regulations or monitoring. Regulated firms and other entities may conduct some business in the shadow banking system, but they are not shadow banks in themselves.

The shadow banking review being undertaken by the FSB does have enormous ramifications. There is a 45-page report of the FSB website, but the main conclusions of the report are:

- A need for a trade repository (what, where and how to be determined)
- Review of haircuts and margins and the ability of a regulator to dictate appropriate levels.
- What is being described as "velocity of collateral". Specifically, the re-use of collateral (re-hypothecation)
- Fire sale of collateral. The stress put on the system when collateral is sold immediately following a default.
- Scrutiny over the practice of offering indemnities to beneficial owners and whether lenders believe this transforms counterparty risk.
- A review of cash collateral re-investment practices, specifically that any losses in this area are typically not shared with the agent and that still, many funds are co-mingled
- Scrutiny of the practices and experience required in pricing collateral (specifically mentions the pricing of MBS and that pricing models were overly optimistic).

Many of the regulations are still in consultation form. Industry bodies such as ISLA are representing the market by lobbying and educating the regulators, who do seem to have a good grasp of the issues. Many banks are lobbying independently, but it is vital that the market understands the issues, what the effects are, and more importantly, what the impacts will be on clients.

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Conversations with...

SLT talks to Helen Baker of Euroclear Asia-Pacific about collateral management in Asia and the swathe of US and EU regulation that could affect Asian business

GEORGINA LAVERS REPORTS

How many custody clients would you estimate are looking at, and taking, collateral management as a standalone service?

There is definitely a renewed focus on collateral management in Southeast Asia. This is partly driven by the plethora of new regulations that capital market practitioners face, as well as the fact that many of the markets in the region are opening up to more international and regional firms. This increase in cross-border transaction activity will require greater amounts of collateral to cover exposures.

It is difficult to put a precise number on how many firms have selected, or are looking at, standalone collateral management services. However, what is interesting is the fact that all client segments are looking at collateral management, ie, national central banks, commercial banks, asset managers, corporates and others. Traditionally, users of collateral management services see a distinct advantage of packaging collateral management and custody services together. While this approach still has advantages, the landscape is changing. At Euroclear, we are working closely with CSDs in the region to supply collateral management services to them. In doing so, these depositories are able to offer their members robust collateral management services in their own domestic markets through their current means of connectivity, without extra development costs.

Firms active in derivative transactions are now considering their options as they realise that a greater number of these transactions will need to be collateralised in the future. These firms include the supranationals and sovereign wealth funds that previously were not required to pledge margins; they will face astronomical added costs if they don't begin to collateralise transactions. In this context, we believe securities collateral will continue to play a significant role.

What's the collateral management market like in Singapore?

In line with many market surveys, while cash is still the most common form of collateral (reflecting that most transactions are executed under International Swaps and Derivatives Association master agreements rather than Global Master Repo Agreements), there is certainly a growing desire to use pools of Singaporean assets as collateral. Furthermore, there is also a growing appetite from lenders to take non-SGD denominated instruments as collateral.

How does Singapore compare to other Asian markets?

Mobilising assets for use as collateral in the domestic Singaporean market, or wider into the international market place, is very easy. There are little, if any, restrictions. Singaporean domestic debt is also highly rated and in demand. Compared to other markets, I would say that if a market has complex tax and account structures, it makes collateral mobilisation far more cumbersome, and so less attractive.

Do you have a wide range of clients, or do you tend to see the same type for your services?

Historically, the need for collateral management services was driven primarily by investment banking, which had the inventory to post as collateral. Today, however, all client segments are seeking experienced, neutral collateral management services. The drivers for collateral usage are also more varied than they were a few years ago. Risk mitigation, scalability, capital optimisation, the use of domestic and international instruments are all front and centre when a firm embarks on selecting a third-party collateral management agent. As a result, a robust multi-currency service is now a 'must have' rather than a 'nice to have'.

What do you understand 'industrial strength' collateral management services to mean, and how does Euroclear offer these?

For me, 'industrial strength' collateral management encapsulates four dimensions: robustness (built on proven technology), mobility (ease of use/access), scale (where the biggest pools lie) and velocity (getting collateral where and when you need it). I would certainly say that Euroclear's offering is industrial strength.

As a world leading group of international and national securities depositories, we hold one of the largest pools of securities collateral in the world. Across the Euroclear group, we currently

hold more than €22 trillion of client assets comprising domestic and international securities.

Our 1,300 clients from around the globe have come to expect us to unlock the full potential of the assets they entrust with us. It is our role to mobilise securities collateral from across the different Euroclear group entities in the safest, smoothest and most efficient way. Our collateral management offering is, in effect, a cost-effective in-sourcing model spanning a wide spectrum of asset classes and exposure types. Both counterparties to the deal remain in full control of their assets throughout the life cycle of the transaction. What is more, Euroclear's industrial strength securities allocation and substitution engine ensures that the pre-defined eligibility criteria set by the two counterparties are respected at all times. For example, should certain securities being used as collateral be needed for trading or settlement activity by the collateral giver, we will automatically remove them and substitute others that are equally acceptable to the collateral taker.

The implementation of new regulations such as EMIR and Dodd-Frank is also prompting our clients to think about the collateralisation of CCP margins. In order to fulfil these new collateral obligations, they will have to either invest in acquiring eligible collateral or find a way to transform the assets they have into CCP-eligible collateral, for example, through collateral upgrade transactions. Euroclear is on hand to assist in these collateral swaps, making non-eligible collateral eligible.

We also continue to support our clients as they work with central bank-based liquidity. A recent example in Europe is Euroclear France's cooperation with Banque de France in managing collateral flows for the central bank's open market activities. Essentially, Banque de France has in-sourced our collateral management service to help manage securities received as collateral from French banks in return for credit. We predict this practice will become a trend in the way collateral management service providers such as Euroclear Bank can help local market infrastructures unlock liquidity, including within the Asian markets.

Is robust technology or client relationship management more important?

In today's environment, we have no choice but to have both at top performance levels. Euroclear has always attached great significance to robust technology—both on a functional and up-time basis. Sound customer relationships have also always been important to Euroclear, but in today's ever-increasing competitive marketplace, customer service is becoming the defining factor.

As a capital market infrastructure service provider, it is no longer enough to support the status quo; we must work with our customers to deliver services that will support their changing business dynamics. That's one of the reasons why we increased our presence in Asia by opening an office in Beijing and adding more client service staff in Hong Kong. We are fully able to serve our local clients, speaking their language and in the same time zone.

Is regulation as much of an issue in Asia as it is in Europe?

The pendulum of regulation is swinging to a more prescriptive environment, particularly in Europe. In Asia, new or increased regulation is less prominent. For one, Asian institutions already shored up their balance sheets after the regional crisis in the 1990s and second, inter capital market convergence is not as advanced in Asia as it is in Europe. Let's remember that Asia operates with multiple currencies and under different market rules and practices—all of which are a challenge when investing across borders.

That said, Asian regulators are actively asking market participants for their views on how the local capital markets could better adapt to the new environment where more and more asset class transactions are centrally cleared. We are actively working with infrastructure service providers in the region to support both domestic and cross-border settlement of transactions and collateral management. Our recent announcements with HKMA and Bank Negara Malaysia are testament to this.

Even though Asian firms are not directly subject to the new EU and US regulations, Asian financial institutions will need to meet many of the same requirements if they wish to continue dealing with counterparties in these markets.

How have you seen SGX's central clearing platform affect the market in Singapore?

The introduction of a CCP, whatever the market, aims to mitigate risks for counterparties conducting securities transactions. The same is true of Singapore. SGX has taken a pragmatic approach and not only accepts SGD-denominated securities, but also highly rated, liquid foreign securities as collateral. This approach underscores the international flavour of the Singapore capital markets.

As not all institutions are inherently long on SGD-denominated collateral, accepting other assets as collateral makes Singapore even more attractive for international market participants. However, as more products are moved on exchange, it makes sense (within sensible risk parameters) to extend the range of eligible collateral to ensure that there is no shortage. Furthermore, the need for a collateral management partner like Euroclear Bank to support the effective and swift mobilisation of collateral will be key to supporting the growth and reducing the cost of margining for international clearing members. **SLT**

Helen Baker
Director of collateral and post-trade services
Euroclear Asia-Pacific

Collateral trading comes of age

Igor Salzgeber of Apex Collateral, which is SunGard's capital markets business, discusses the age of collateral management optimisation

COLLATERAL COMMENT

The collateral management function is in the process of moving from a predominantly back-office operation activity further up the value chain. It is becoming a front-office function, helping to protect and drive revenues for an organisation. Since the financial crisis, the importance of effective collateral management has come to the forefront of profit and loss concerns.

At the same time, volumes and spreads in traditional securities finance markets have dropped significantly, and as a result, overall revenue that could be achieved from traditional securities lending has also decreased. The focus on efficient commercial use, or reuse, of collateral that is held on a firm's books has become a necessary, compensatory function, and one that is in some ways helping to offset the melting away of revenues from more traditional securities finance business.

Research conducted in 2011 concluded that as much as 15 percent of a firm's collateral is either unused or under-used, representing an opportunity cost of approximately €4 billion per year. These figures underline the importance of centralised inventory management across products and asset classes combined with sophisticated collateral trading capability.

Trading's role in collateral optimisation

Collateral trading needs to work in conjunction with collateral optimisation to be most effective; not only to satisfy a particular collateral demand, but to do so with the best possible allocations to hold down the cost of collateral, and maximise trading revenues.

The main areas of collateral management—operations, global inventory management and collateral trading—require efficiency and automation in order to work together cohesively. Working in conjunction with the centralised, global inventory of assets is collateral optimisation, which helps collateral trading to determine the best positions to be freed up and allocated in order to optimise the use of collateral and take better advantage of collateral for funding or financing purposes.

The introduction of new liquidity standards and increased margin requirements have resulted in collateral demand increasing, while at the same time, supply has dropped due to tighter eligibility criteria and limited options for re-hypothecation. Recent industry studies have shown that the larger the pool of collateral assets held across trading books and business lines, the greater the opportunity to use these collateral positions to generate additional revenue. Accessing this additional source of revenue can, however, easily backfire by focusing on only one part of the problem. A holistic approach on the use of collateral across business lines, without compromising any regulatory or business constraints, will yield the targeted result.

The transition of some of the tasks that are related to the monitoring of collateral, as well as greater visibility into these details—reporting, processing of margin calls and returns, collateral substitutions, notification of corporate events and processing of securities transfers—to the trading area is in direct response to the need to optimise collateral for profit.

While many of the tasks that were originally associated with effective management of collateral remain with the operations group (margin calls, settlement/fails management, corporate actions), certain functions (returns, re-allocations) have transitioned to the collateral trading area. This provides maximum visibility and awareness of the current and upcoming potential changes to collateral positions (potential substitutions, upcoming corporate actions, hard to borrow indicators), ensuring collateral can be optimised for profit.

Convergence of operations and trading functions

To make the transition, organisations are looking to establish new teams—often within the securities finance area—responsible for trading collateral. The responsibilities go far beyond the traditional operations function of managing and processing collateral positions. This new paradigm requires the ability for trading desks to gain greater insight, not only into the collateral that the firm has on the books, but into the underlying exposures and transactions as well.

Firms need to be able to anticipate the needs and challenges of the trading function within the context of collateral management. In addition, the more 'liquid assets' the regulators and other institutional bodies require from firms to remain active within a certain trading space, the greater the requirement to all available assets—with the help of a sophisticated trading capability.

At the same time, operational tasks associated with collateral management need to be as automated and efficient as possible to help establish a more proactive risk management environment. From the traditional collateral management perspective, the back office role is to reduce exceptions, power risk management and help the firm to anticipate the possible impact of liquidity or counterparty changes. Today, those back-office functions need to be highly automated and efficient, making it possible for collateral positions to be viewed and managed across multiple business silos in order to provide the consolidated view of data needed by the front office for trading purposes.

Are we heading in the right direction?

The key advantage of a tighter relationship between the front- and back-office is the ability to view and manage collateral trading from a global perspective, facilitating the re-use of collateral across business lines, geographies and organisational functions. This opens up the opportunity for 'interesting' assets to be received as collateral, such as stocks that might be 'special' or 'hot', or those of key interest to a particular trading desk, to be used or re-used. It also provides a platform from which automated, mathematically-based collateral optimisation proposals can be made, which are based on a firm's own specific priorities and preferences.

Cross-enterprise collateral solutions, encompassing functions to support trading and operations, are best equipped to manage the shifting focus on collateral management functions from the back-office to the front-office. In this new environment, the trading component becomes an extension of collateral management operations in the back-office. As a result, collateral trading becomes a proper discipline on its own, helping to empower securities lending or repo areas to generate higher leverage and P&L on collateral positions that are held on a firm's books.

The traditional collateral management function has matured with increased efficiency and automation since the financial crisis. As a result, this is changing the landscape and resulting in an even closer relationship between securities finance and collateral management areas, in some cases leading to the merging of front-office and operational activities, and the sharing of ownership of P&L for collateral positions. **SLT**

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Collateral thinking

SLT's panel of collateral management experts dissect the business of collateral and examine why 'collateral optimisation' is on everyone's minds at the moment

Olivier de Schaetzen
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Euroclear

James Malgieri
head of global collateral management and securities clearance services
BNY Mellon Broker-Dealer Services

Jonathan Philp
specialist in collateral management
Rule Financial

Arne Theia
managing director and head of repo and collateral trading
UniCredit Bank

Nick Newport
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InteDelta

Paul Wilson
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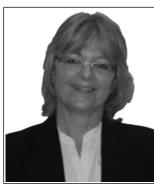

Jane Milner
head of strategy and enterprise collateral management
SunGard's capital markets business

To what extent are transactions becoming more collateralised?

Olivier de Schaetzen: We are definitely seeing more collateralised transactions. Growth is coming from all directions across the various segments that we cover in triparty. In the repo segment, we are seeing significant inflows of business from firms looking to collateralise exposures arising from their money market investments. With capital preservation on the top of their priorities, firms are turning to repos, particularly triparty repos, to achieve this objective. Investment managers and corporate treasurers represent the majority of new client types that we are welcoming to triparty.

In the securities lending segment, we are observing a strong trend towards the use of non-cash collateral in these transactions, which for the first time account for more that 50 percent of triparty securities lending volumes. Last, but not least, we are experiencing strong growth in derivatives-related collateral management, indicating a willingness by transactional parties to increase the use of securities as collateral in preparation for the implementation of new regulations, such as EMIR (European Market Infrastructure Regulation) and Dodd-Frank.

James Malgieri: The current regulatory changes are consistent on this: collateral, the need for more collateral and the right type of collateral. The unsecured cash market has more or less disappeared. Any sustainable finance activity now needs to be collateralised. We have, at the same time, worked with institutions that use collateral management to broaden the types of securities for securities lending and derivatives transactions, both OTC (over-the-counter) and cleared.

To isolate growth to a single factor and remove other market cycles is not only challenging, but limiting in its approach. We are running record high collateral volumes and every week it is increasing—there is a clear and strong trend.

Jonathan Philp: Collateralisation is widely seen as the most practicable way to manage counterparty credit risk. New regulations including Title VII of the Dodd-Frank Act and the (broadly) equivalent EMIR prescribe detailed collateral requirements for cleared and bilateral OTC derivatives exposures.

The growth in demand for collateral is therefore coming from: (i) new derivatives regulations, as many OTC derivatives participants have not historically been required to provide collateral for initial margin; (ii) the spill-over of these regulations into the secured lending markets, which are used by market participants to source central counterparty-eligible collateral: and (iii) a generally more conservative approach to the control of counterparty credit risk, such as reduced willingness to allow re-hypothecation collateral assets.

Arne Theia: There is a clear trend towards collateralisation that is mainly driven by upcoming regulations. To mitigate risk as much as possible, regulators generally promote secured transactions while penalising unsecured ones, making them uneconomic for banks. EMIR will have a huge impact on client clearing as transactions have to be fully collateralised and mainly executed against CCPs. ISDA estimates additional collateral demand for the clearing of OTC derivatives has reached $3 billion. Basel III will dramatically increase funding costs for unsecured transactions or secured transactions with lower quality of collateral.

Nick Newport: There is a clear growth in collateralisation across all areas of the industry. One of the primary elements of the regulatory response to the financial crisis is for more collateral to be held, particularly in support of derivatives trading. In particular, initial margin will now need to be provided to support derivative trading in far greater amounts than has ever previously been the case. This will equally affect both cleared derivatives and the remaining non-cleared derivatives. When taken together with other aspects of regulatory reform, such as restrictions on re-hypothecation, this will have a major impact on the industry.

Jane Milner: Although we are not directly active in the markets, we are aware that there has been an increase in the use of 'secured' funding transactions, and the repo markets have been the most visible beneficiaries of this growth. In terms of collateral to support the underlying transactions, collateral margins have increased, resulting in the demand for more collateral (value). The ultimate move towards CCP structures, either because it is mandated or to take advantage of the beneficial capital treatment that they bring, will further increase the demand for collateral as all parties need to put up margin/collateral when trading there.

Is the securities finance market benefitting from an increase in activity?

Philp: Yes it is. OTC derivatives users are being forced to put up significant incremental collateral to meet initial margin requirements. The range of eligible collateral, whether for cleared or uncleared trades, is narrow and likely to remain that way. OTC derivatives users that are not necessarily natural holders of CCP-eligible collateral need to source securities that will be accepted, and they will look to the repo and stock-borrow-loan markets to transform less liquid assets, such as equities, corporate bonds and so on, into CCP-eligible collateral. From an OTC derivatives perspective, this means incurring additional counterparty credit risk and potential over-collateralisation through multiple haircuts, but it is likely to drive higher volumes in the securities lending markets.

Theia: It opens up a new playing field for the securities financing industry as it is getting more important to source, transform and optimise collateral. Unfortunately, new regulations will affect the repo and securities lending markets and make them more difficult and expensive.

Malgieri: The securities finance market is both benefitting and suffering from all of the ongoing changes. While keeping up with all of the investments that need to comply with changes is a challenge, it is clear that market activity is increasing. There is an increase not only in straight repo financing, but also in collateral transformation. If we include securities lending in securities financing, we anticipate increased activity in collateral trading in the form of borrowing one asset to be used as an eligible asset and posting other assets as collateral.

> Newport: One of the primary elements of the regulatory response to the financial crisis is for more collateral to be held

de Schaetzen: New entrants to the repo market, such as corporate treasurers, are coming with term money across the money market curve, which dovetails perfectly with the trend that we see of the banks and dealers looking to extend their funding horizons to comply with new regulations. In addition, the growth in collateralised transactions across business lines is building the business case for centralised collateral management functions.

Milner: In an environment where more high quality collateral is required, for example to support what were previously OTC derivative transactions moving to CCP, 'collateral transformation' trades will become more prevalent. Those needing to deliver high quality collateral will drive demand for assets typically held by pension funds and other institutional investors. The hurdle is of course getting conservative funds to lend out their prized sovereign debt against cash or equities; collateral they typically would steer away from.

Is the type of collateral being accepted changing?

Paul Wilson: There are three elements to this. Firstly, there is a greater consideration of using securities rather than cash as collateral. Following the problems with cash reinvestment during the economic crisis, the view that non-cash can provide an effective means of collateralising trades has gained traction.

Secondly, the range of eligible collateral that firms are accepting is in some cases becoming broader. Some firms are now accepting more corporate bonds and equities as collateral. This is partly because firms that have implemented effective collateral management systems can be more confident that their haircut and margin calculations, and eligibility and concentration criteria, are accurate based on the credit risk of the counterparty and quality of the collateral they are taking in. Collateral optimisation also allows firms to allocate lower rated assets more effectively to counterparties who will accept them as collateral.

> Wilson: The range of eligible collateral that firms are accepting is in some cases becoming broader. Some firms are now accepting more corporate bonds and equities

Finally, in the light of current eurozone and sovereign debt crises, institutions with access to both large shapes of high quality, hard-to-borrow assets and systems offering sophisticated collateral management controls have the opportunity to lend these assets out versus a set of collateral schedules with differing risk levels in terms of eligibility, haircut and concentration components. This provides the market with increased liquidity. It also offers the lender an optimised revenue stream with lending rates correlated to the risk of the chosen collateral schedule, and provides both parties with clearly defined risk mitigation strategies.

Malgieri: The appetite for collateral and asset classes changes constantly. The collateral that is used is often a reflection of the risk appetite in the system, and it is also a function of the supply of collateral. For example, with the recent downgrades in Europe we are now seeing an increased interest in Japanese government bonds as collateral in the programme, as their relative rating has increased. We see shifts in asset classes depending on underlying trading strategies that may make one asset class more available since it is held as a hedge. Regulatory changes also play a very important role.

de Schaetzen: The quality of collateral that is used in our triparty collateral management environment continues to increase, with 55 percent of the total value of collateral rated AAA and 96 percent investment grade. However, the growing need for quality collateral is driving the market to long-term collateral swap transactions where firms are exchanging quality collateral against less liquid assets. We expect this segment of the industry to significantly grow in the future as the demand for quality collateral continues to increase with the implementation of new regulations.

Philp: There has been much discussion of the 'collateral crunch'; a shortage of high-quality liquid assets due to the competing demands of the new Dodd-Frank/EMIR collateral requirements and Basel III liquidity rules. Clearing house collateral requirements in particular are very restrictive, but a much broader range of collateral can be used in the repo and stock-borrow-loan markets. The primary function of a clearing house is to concentrate and manage counterparty credit risk, and clearing houses are systemically significant because of their role as central counterparty. I don't expect to see a material loosening of collateral eligibility standards. It is possible that some additional asset classes, such as investment grade corporate bonds and gold, for example, may be accepted. Some CCPs accept highly-liquid equities, but only subject to substantial haircuts.

Milner: Anecdotally, we hear that lenders are becoming more flexible and borrowers are delivering increased margin values on collateral types such as equities. Lenders that are more flexible with their collateral requirements will be the ones that make more returns on their assets. Of course, managing a set of diverse collateral types ever more closely, especially as some would argue the collateral transformation trade (collateral downgrade from a lender point of view) increases risk, a lender will require ever more intelligent management of their collateral in order to benefit from the incremental revenues.

> de Schaetzen: The quality of collateral that is used in our triparty collateral management environment continues to increase

Theia: Basel III is going to change our collateral universe. We will face new regulatory asset classes: entirely accepted, partially accepted and not accepted by the regulator. Non-regulatory assets, such as equities, will lead to higher funding costs for banks and may be banned from collateral schedules.

Are you seeing more of an interest in the use of CCPs in the securities finance market?

de Schaetzen: Yes, and the trend towards greater use of CCPs in the securities finance market will continue, as new CCP initiatives are coming to the market for both the repo and securities lending markets. The modest success of CCP services to trade collateral baskets on a screen, such as the EuroGC products, is very likely to accelerate when the necessary technological investments have been made by market participants. So far, CCPs have not yet proven their business case for use in the securities lending market for various reasons, of which a significant one is the challenge of adapting the CCP model to the specific requirements of the securities lending market. It will be very interesting to follow the new initiatives that are in the pipeline.

As far as the derivative market is concerned, CCP collateral management will inevitably be at the forefront, particularly for buy-side firms, as most, if not all, derivatives transactions will soon start trading on exchanges.

Malgieri: We do see a large interest in CCPs, particularly in the derivatives clearing space, but also in the funding and securities lending space.

In the derivatives clearing space, firms are actively working on the effects of upcoming regulatory changes. There is a well-established estimate of $2 trillion representing the worth of collateral that is expected to be needed if all OTC derivatives trades are cleared through a CCP.

> Philp: The triparty model, which is well-established in repo and securities lending, can be seen as an incremental step towards central clearing

However, this is only one of the trends in the market. In the derivatives space, there are several other trends that are in force: the request to segregate margin; concerns of transition risk; transparency not only on trades but also on collateral pools; CCP collateral acceptance; worldwide downgrades of sovereign debt; and acceptance of corporate bonds.

In the future, collateral managers need to do more with less collateral. That is, in an environment with fewer resources, collateral should be used most efficiently. For this to work effectively, the process in derivatives collateral has to be seen as an end-to-end process; it needs to encompass the buy side, the sell side, the CCP and potential third parties for collateral transformation. To meet a $2 trillion margin call, all collateral needs to be considered, including the need to transform collateral.

Wilson: This is something that our customers and prospects are starting to ask us about and that 4sight is actively engaged in. Should this model become prevalent in securities finance, firms will require collateral management solutions that can support CCP margining on a real time, intra-day basis. As well as connectivity with a range of CCPs, collateral management systems will need to be able to accurately forecast future margin requirements across products where appropriate based on each CCP's margin calculation criteria.

Users will also require a consolidated view of collateral across all trade types (eg, securities lending, repo, derivatives), and indications of which trades can be centrally cleared, triparty or bilateral. We are therefore working with European CCPs to determine their rule sets and margin call protocols for a range of cash, derivative, and collateralised trading activities. This in turn will increase our ability to satisfy cross-asset class or cross-business line collateral netting and optimisation.

Philp: There are signs of interest and indeed there are facilities in the market to clear repo transactions. The main regulatory focus is currently on the completion of the overhaul of the OTC derivatives markets, a key feature of which is the imposition of the CCP. The process of migrating from a bilateral to a cleared market is challenging; for example, the assets that are traded have to be standardised to allow clearing to be practicable. Regulators evidently regard the cleared model as superior in terms of risk mitigation and transparency, and so securities finance market regulation may well follow suit in due course. The triparty model, which is well-established in repo and securities lending, can be seen as an incremental step towards central clearing.

Theia: Regulators are promoting CCPs by making bilateral business more expensive. But there are other advantages of using a CCP, including risk mitigation or improvement of operational efficiency. Also, electronic trading is much easier against a CCP.

As collateral management has evolved into collateral optimisation, can this part of an institution's activities now be considered a profit centre?

Ted Allen: The increased pressure on firms to make the best use of assets is causing many to re-evaluate what was historically an ad hoc and often back-office activity. Collateral management is moving front and centre to the organisation with many realising the significant cost reductions that can be possible through an active management of collateral. Collateral optimisation has emerged as a new front-office discipline mandated to make the decisions around allocations of assets with specific P&L against this function.

de Schaetzen: Given the scarcity and fragmentation of collateral pools, managers who are able to optimise a firm's collateral resources efficiently and in a scalable way will become stars. Collateral is clearly becoming the blood of the financial markets, with collateral management at its heart.

Malgieri: Collateral optimisation is a very wide topic, and it is also a very subjective topic. It can cover many topics, including collateral management, identification, transformation and trading. Depending on how you view collateral optimisation, as a user, as an agent, or as a principal from the buy side or for the sell side, you will receive different answers. Today, there are already collateral trading desks that operate as profit centres, so it will be up to each business area to define how it structures their desks and business.

Wilson: From our perspective the move to actively pursue such centralisation is still in its infancy. This is partly due to the complexity, cost and cultural change of bringing together such disparate or previously siloed business lines. It is also due to internal commitments to bringing CCP functionality online, partly because of uncertainty about the actual impact of CCPs, in addition to unclear regulations. Finally, many institutions are still playing catch up, being simply focused on implementing basic collateral management fundamentals.

In some forward-looking firms, however, collateral management is certainly moving from a siloed middle- and back-office function to a front-/middle-office activity that's centralised across business lines and geographical regions.

Philp: While the emphasis of investment in active collateral management is, in general, directed at minimising the cost of sourcing and delivering collateral to support trading and hedging strategies, the most sophisticated banks are actively trading their collateral inventory, particularly in the repo and securities lending markets, to generate profits. In some respects, the direction of regulation weighs on this by requiring some categories of collateral to be locked up at third-party custodians, which clearly limits the scope for its profitable re-use.

There are clear opportunities for revenue and profit generation for providers of collateral management tools and infrastructure, as well as triparty collateral agents and clearing brokers with the capability to offer collateral transformation services to their clients. However, collateral transformation is likely to be a relatively costly service to run, and at a time when banks face more stringent capital requirements and difficult market conditions. Buy-side institutions that expect their clearing brokers to upgrade assets to CCP-eligible collateral on their behalf may instead be forced to enter the repo and securities lending markets directly.

Newport: Before elaborating on this, it's worth reminding ourselves that the primary reason for collateralisation is as a risk mitigant and this has not changed. So the way in which collateral management has recently evolved within financial institutions now has a number of objectives.

Firstly, to ensure that collateral does serve its purpose as the first line of defence against credit risk losses. Secondly, in managing the collateral process from an operational perspective, ensuring that this is done is as streamlined-a-way as possible. Finally, to make use of available inventory to minimise the collateral financing costs to the organisation.

This third element is an area that might be seen as a profit centre and does lend itself to the setting of P&L targets. But, for the majority of firms, I would say that they view this function less as one of maximising profit potential but rather minimising financing costs. The difference is subtle but important, and should be seen in the light of the new regulatory environment that has culminated in a significant rise in the amount of collateral, formed of a limited pool of high quality assets, which institutions need to place—and therefore also to finance. The driver for most firms in setting up collateral optimisation processes is primarily a defensive reaction to this increased collateral burden. Effective optimisation will without a doubt be critical to the ongoing ability of institutions to continue to trade derivatives in a cost-effective way.

What does collateral optimisation actually mean to you?

Theia: It's all about using collateral as efficiently as possible. It is important to know exactly what your firm's collateral, funding and regulatory positions are, and then to reuse and exchange your collateral to match existing requirements.

Newport: The term collateral optimisation has often been used in many different ways over the years. Sometimes, to refer to the operational streamlining of the collateral process, and at other times, to refer to the efficient management of collateral inventory. There now seems to be a convergence in use of the term across the industry to mean optimisation of the use of inventory for collateral purposes.

> de Schaetzen: We are bringing innovative solutions to extend the reach of collateral that our clients can use to cover exposures in a triparty environment

Optimisation of inventory though can also mean different things to different people at times. For some people, this can mean re-using collateral assets in the most effective way possible to maximise return. To others, and I think perhaps more commonly, it is used to refer to maximising existing inventory to meet collateral requirements as effectively as possible. There is no contradiction in these different outlooks, and they are really two sides to the same coin.

Even within either of these approaches, the exact way that any given organisation will wish to optimise will differ based upon many different parameters—for example, cost of funding, haircuts, shapes, minimum lot sizes and exclusion of specials. These many variations on the theme of collateral optimisation mean collateral optimisation technology solutions need to be as flexible as possible.

de Schaetzen: Collateral optimisation is a key driver of the services that we offer to our customers. We do whatever we can to help our clients to make the pools of collateral they entrust to us work harder for them. We create new collateral optimisation features regularly that surpass market standards and provide even better results with greater levels of granularity.

In addition, we are bringing innovative solutions to extend the reach of collateral that our clients can use to cover exposures in a triparty environment. A recent example is our partnership with BNP Paribas Securities Services, as a domestic agent, where our mutual clients will be able to mobilise collateral held in BNP Paribas to Euroclear Bank to use as collateral in triparty. Once the triparty transaction is closed, the assets will be returned to their account in BNP Paribas. This service will be launched in June, and soon thereafter, we will expand the service to cover more agents and markets.

Malgieri: From our perspective, we look at collateral optimisation as a process that brings efficiencies and mobilises collateral for our clients and allows them to ensure that collateral is allocated at the right place and at the right time.

Allen: There are many different aspects to the question of collateral optimisation. It is important to look at the problem from the firm perspective rather than at the level of the individual silos

Wilson: At 4sight, we see collateral optimisation as the centralisation of collateral management and optimisation into a profit centre, or 'collateral hub'. This allows institutions to keep a tight control of collateral risk and collateral usage costs on an enterprise-wide basis. From there, firms can optimise use of collateral inventory across a number of different trading opportunities and business lines, both internally and externally.

As firms gain a clearer picture of their true cost of collateral in P&L calculations, they can then use this to more accurately assess the profitability of a given trade, versus other trades. This ultimately results in them making more informed trading decisions in real time.

On the flip side, a centralised approach to delivering RQVs or margin calls is an important part of the optimisation process. This allows firms to validate exactly what collateral they receive to cover exposures across multiple business lines—whether via CCPs, bilaterally or via tri-party collateral allocations.

Matching collateral receipts to original RQVs, exposure calculations, collateral schedules and risk metrics helps to manage risk, cost and collateral re-use. It also provides a means of correlating underlying client demands for individually-tailored collateral schedules with real-world collateral that comes from brokers under their more generic schedules.

In a nutshell, collateral optimisation is the ability to calculate the opportunity cost of collateral and then use this information to mitigate risk, while reducing the cost of collateral across business lines that the firm is engaged in. Collateral optimisation provides a driver for more profitable trading strategies, all on a more real-time basis, effectively managing the supply and demand for collateral on an enterprise-wide basis in the most efficient manner possible.

Philp: Collateral optimisation is about minimising the opportunity cost of allocating assets as collateral, compared to possible alternative uses, such as trading or funding. The two prerequisites of effective collateral optimisation are: (i) a comprehensive view of current and projected liabilities that require collateral across all products and markets; and (ii) a corresponding view of assets available for use as collateral, including collateral received that is available for re-use, and proprietary positions. The optimisation process then allocates available assets to collateralise particular liabilities at minimum cost. This is non-trivial, as counterparty eligibility criteria, concentration restrictions, haircuts and alternative opportunities for deployment of particular assets must be considered. However, the systematic application of rules or algorithms to the collateralisation problem can generate substantial efficiencies. Optimisation can, in practice, range from very sophisticated algorithms that are run many times a day to a relatively straightforward preference ranking of assets that determines the order in which they are deployed to meet margin calls.

Allen: There are many different aspects to the question of collateral optimisation. It is important to look at the problem from the firm perspective rather than at the level of the individual silos. The overall goal of collateral optimisation is to reduce the total cost of collateral of the firm as a whole and this is achieved through a number of methods:

- Reducing the amount of collateral that is demanded through optimising the netting set for each collateral call. For example, CCPs are starting to offer this service to net futures exposures with OTC derivatives, which gives the opportunity to take greater advantage of portfolio effects.
- Renegotiating bilateral collateral terms to allow for a more advantageous set of assets to be used as collateral.
- Optimisation of the collateral allocation. This is much more than cheapest to deliver for an individual call; it involves looking at the total set of collateral call requirements and allocating the collateral using complex optimisation algorithms to give the maximum overall benefit.
- Collateral optimisation requires firms to actively manage the collateral they have posted out and perform substitutions as the optimal deployment profile changes over time. These collateral trades and movements should be automated as much as possible to reduce the operation burden and risk.

How is technology changing the way collateral optimisation is being carried out?

Malgieri: The more proactive firms are considering collateral location on an intra-day basis, and we work with our partners to assist them in this process. Collateralisation techniques need to meet peeks of exposures in different regions and at different times. I would not rule out that there will be a need to transform collateral on an intra-day basis. The technology must continue to evolve to allow for firms to have a central view on their collateral they have and need. In the event that firms do not have the desired collateral, they will need to know the price to obtain it on an intra-day basis. Forecast technology needs to evolve to accommodate and predict the collateral demands across all product sets including, but not limited to, derivatives trades (both OTC and CCP), cash equity trades, settlement, payment systems, repo trades and securities lending trades. Collateral is now used in almost every transaction in the financial system.

Malgieri: The more proactive firms are considering collateral location on an intra-day basis

Allen: Increasingly, there is demand for technology that will work at the enterprise level across silos. While there are often internal barriers to acting off a single asset pool, many firms recognise the strategic need to take this leap. A global, real-time cross-asset inventory is a vital tool in determining the set of assets that can be deployed. An asset can have many uses of course, covering liquidity funding ratios, use for trading, and deployment as collateral against a number of different underlying transaction types.

The technical solution to determining how best a set of assets can be deployed then becomes a large but solvable technical challenge. Collateral optimisation tools are now offered that can crunch large portfolios against large sets of collateral requirements and determine the optimal allocation on a holistic basis. The use of such tools opens up the possibility of minimising the cost of collateral, as it takes away a significant burden on expensive front office resources that may previously have had to calculate the collateral allocation and book the collateral trades manually.

de Schaetzen: Both state-of-the-art technology and sharp expertise are required to further optimise collateral management. As an in-sourcer of collateral management services, we are committing significant resources to the development of technology as an enabler of collateral optimisation. Our collateral user group is extremely helpful in helping us to set the right priorities and define the right technological changes to deliver what our clients need in this fast-changing environment.

Philp: Both the need for comprehensive views of assets and liabilities are challenging to implement; product silos must be aligned, disparate sources of data integrated and business processes and technology solutions designed and/or selected. If the data can be assembled, then the challenge is to design and implement an efficient and cost-effective algorithm; one that can compute sufficiently robust collateral allocations without excessive performance penalties, in terms of time to compute and implement a given allocation.

Current enterprise data management tools and techniques are also key enablers of enterprise-wide collateral management, as they help to align and normalise data drawn from legacy product or infrastructure silos.

Wilson: Technology is helping to give firms a clearer, more consolidated real-time view of inventory and collateral usage across business lines for current and future dates. Another key building block is the ability to accurately model increasingly complex collateral schedules, including costs, haircuts, margins thresholds, collateral eligibility and concentration criteria to a very fine degree of sophistication. This forms the foundation of optimisation.

Once this structure is in place, collateral management systems then give users the capability to accurately manage and report, in real-time, the subtleties of collateral management, exposure and margin call workflows for asset classes including—but not limited to—securities lending, rebates, repos, CSA, long forms, ETFs, and FX, whether bilateral, or via CCP or triparty.

Finally, technology systems are providing users with the ability to simulate a range of collateral optimisation scenarios at trade, book, strategy, and programme level. Users can then turn these simulations into real collateral movements on-demand to structure and restructure any given collateralisation requirement. Because of the complexity and multi-faceted nature of these processes, technology solutions are the only way to achieve these activities successfully.

Newport: Technology is fundamental to the process of collateral optimisation.

The first technology challenge that is faced by many organisations relates to data integration and aggregation. Without a clear view of inventory, collateral requirements, eligibility and other reference data in a timely manner, optimisation is impossible. A number of collateral technology vendors are developing solutions specifically targeted at addressing this data aggregation challenge.

Having achieved a clear and timely view of inventory, technology is also critical to actually running the optimisation process. This requires a flexible framework enabling end-users to configure their optimisation preferences, an algorithm that arrives at the 'optimal' answer in as fast a time as possible, and straight through processing to effect any asset movements with as little operational overhead as possible.

It's fair to say that most institutions are only at an early stage of implementing their technology solutions in many of these areas.

Is the old system of silo-based collateral management now being consigned to the history books?

de Schaetzen: Silo-based collateral management is, unfortunately, still a reality for many firms and service providers. Some firms have combined and centralised all of their individual collateral management functions. They are now reaping the benefits of such a strategy by having easy access to collateral that was otherwise fragmented. Those using Euroclear Bank's triparty services can maximise our collateral optimisation features better than those firms that have not centralised, as their assets can be allocated very efficiently across exposures arising from many different business lines. These include repos, securities lending, derivatives, CCPs and open market operations with central banks.

> Newport: Without a clear view of inventory, collateral requirements, eligibility and other reference data in a timely manner, optimisation is impossible

Newport: Most organisations are continuing to push forward with some form of cross product integration of collateral management. Such integration can be undertaken in different ways though and there may not be a 'one size fits all' answer that is right for all institutions.

At the very least, integrated collateral reporting across the various product silos is essential. This serves both client reporting and internal risk reporting purposes. One of the key needs emerging from the financial crisis is for institutions to be able to generate an aggregate view into all collateral holdings at the click of a button. This is the minimum level of integration that firms are undertaking.

Operational and technology integration across the product silos is also happening, bringing together derivatives, repo, equity finance and exchange-traded derivatives, and margining processes into central organisational units using standardised processes and standardised technology architectures. Different firms take different views on how deep such integration should go, depending on perceived cost benefits. The trend is certainly towards greater integration though.

Finally, from a front-office perspective, the more aggregation of inventory that can be achieved across products slios, the more opportunity for effective optimisation.

Malgieri: The current systems are working very well. In fact, some of the technologies that are already built prove a very efficient base for further developments, and they need to be employed across silos. The current platforms are already very robust and there are continuous improvements to make them even stronger. Most of the work to truly optimise collateral is organisational and not systemic. While the system can help, the greater challenge will be changes in the governance, including transfer pricing of collateral with maintained risk profile. These changes need to come from within the organisations.

Wilson: For some companies, a silo-based approach works well, but for others cross product is clearly more effective and profitable in the current market.

Philp: This is a challenging process, demanding new approaches to organisational, process and technology infrastructure design. Collateral management often evolved as a residual operational function within product silos. The sophistication of each product-specific collateral management process reflects the relative importance and maturity of the product within each institution. Furthermore, collateral management tools have evolved within product silos, addressing market-specific processes. Only now are vendors starting to offer genuine cross-product collateral management capabilities that can support true enterprise collateral management.

Theia: Efficient management of collateral requires full transparency and availability of a firm's inventory. Centralising and pooling assets helps to optimise collateral and save costs. But complexity grows, which means sufficient technology is essential.

Allen: In most institutions, collateral management has evolved independently in product silos and only now are they attempting to move to a centralised view. There remain significant organisation challenges in many firms to moving away from silos and it requires direction from the top layer to create an enterprise level function that is tasked with optimising the use of assets. For many this will be a gradual process as business lines are merging. We are seeing it in pockets with listed cleared and bilateral derivatives and we see it with financing activities, but for many, particularly the larger institutions, it remains a theoretical ideal. Of course, it must be stated that there is still scope for optimising within the product silos and optimisation tools and costs can be shared.

How do you see the market developing in the future?

de Schaetzen: Our view, which is supported by recent market studies, is that astute collateral management will play an increasingly crucial role in financial markets. The biggest concern is the potential shortage of quality collateral as demand grows. New banking regulations and the migration of OTC derivatives to exchanges alone will create an immense need for quality collateral. Banks and buy-side firms will need to optimise all available pools of quality collateral and will need to secure their access to sources of quality collateral by engaging in new types of transactions, such as collateral swaps.

Firms that are already actively using triparty collateral management services will further leverage the benefits that are derived from outsourcing their administrative burdens to a triparty agent. This is because most of the features that they have been using for their securities financing activity can also be used for the collateralisation of credit exposures, such as those relating to derivatives. We are confident in the strength and future of triparty collateral management.

Wilson: From a technology point of view, we envisage more automation around optimisation and dynamic margining.

As time goes on, collateral management systems will be able to react in a highly automated way to real time incoming market data feeds. This data could trigger automatic changes in haircuts and collateral eligibility criteria in the system in response to market events, subject to user approvals. Following this, the system could then automatically suggest reallocations so collateral is quickly redeployed in an optimised manner based on these new risk parameters.

This will help firms to respond more quickly and fluidly to market conditions, particularly during periods of volatility and when processing high volumes of trades. It may be that the market also uses other criteria to model counterparty risk, such as monitoring credit default premiums as a means of dynamic margining traditionally controlled by rating bands and forecasts.

Full cross product netting could also become a reality once a standard master netting agreement is formalised. Should CCPs achieve full interoperability at some point in the future, technology systems will also need to provide support for this model and help users to determine the benefit of transacting with each potential CCP from a capital, netting and collateral perspective.

Philp: Market participants have little choice other than to source and deploy eligible collateral assets if they wish to maintain their levels of business activity. Some institutions may scale back their OTC derivatives activities, but in general we see a desire to sustain activity, and therefore, a pressing need to invest in active collateral management. The need to cast the net wider to source eligible collateral leads to a tightening of the relationships and interdependencies between, for example, the repo, stock-borrow-loan and derivatives markets, and this will be reflected in the development of collateral management practices, as well as in the evolution of supporting products and services.

> Theia: The good news is that without securities financing, it will be hard to perform any financial business. And that provides us with a lot of opportunities

Theia: The financial markets are facing a very difficult environment. And that will hit our industry for six. The good news is that without securities financing, it will be hard to perform any financial business. And that provides us with a lot of opportunities.

Allen: The huge weight of regulatory change affecting the industry, including Dodd Frank, EMIR and the parallel implementation of the Basel III capital adequacy framework, represents a significant set of challenges. Firms must address capital and collateral management requirements alongside falling spreads. The evolving regulatory environment seems set to put intense pressure on the liquid assets that will be required by banks and other financial institutions to meet minimum liquidity requirements and collateral obligations.

Realignment of collateral management and collateral optimisation to a central function must continue and it requires consolidation of functions, business processes and technology. The benefits that can be achieved from the active management of collateral are substantial, and support a compelling business case for investment. **SLT**

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Mexico

SLT looks closely at a market that, despite reforms, is still proving remarkably stubborn when it comes to securities lending.

GEORGINA LAVERS REPORTS

When the most recognisable names in the financial industry skirt around the Mexican market, you know it's for a good reason.

There are some programmes in Mexico that are run by local players, but the stalwarts that make up the majority of the sector there—Santander and J.P. Morgan, among others—could not be reached for comment on a market that, despite the best of efforts, is refusing traction on securities lending.

Up until 1994, the only foreign bank in operation in Mexico was Citibank, before the North American Free Trade Agreement (NAFTA) opened the securities markets to US and Canadian firms.

Large international banks, such as BBVA, Banco Santander, HSBC and Scotiabank, along with Citibank, acquired most of the largest Mexican banks and began lending, and are now described by an industry insider as "the most aggressive players on the market".

In 1995, more foreign banks entered the market, including ABN Amro, Fuji and Societe Generale. Tokyo Commercial Bank began participating in 1997 and Deutsche Bank in 2000. Despite the industry being more than a decade old, many lenders are only now establishing a presence in the country.

A source from Banco de México, who did not wish to be named, says that although Mexico was ahead of its Latin American counterparts in the securities lending game, the finishing line is not in sight.

"We put in place a complete set of regulations to really try and kick-start the market. I don't know exactly how we compare with other emerging markets in Latin America—my feeling is that they are not that developed. At the Central Bank we examine international research and securities lending. What we do is see what procedures are in practise in developed markets, and how we can apply these principles to the Mexican securities lending market."

Mexico reformed its pension system in 1997, transforming it from a pay-as-you go, defined benefit scheme, to a fully funded, private and mandatory defined contribution scheme. The reform was modelled after the pension reforms in Chile in the early 1980s and was a result of recommendations from the World Bank. The comprehensive set of reforms that Mexico has implemented since the middle of the 1980s has changed the evolution of the country's economy. The period of economic reforms from 1987 to 1993 was one of the most intense in the country's experience. Among other reforms, the external debt was renegotiated, many government enterprises were privatised, a profound fiscal and financial reform was carried out, and greater attention was paid to foreign trade as a source of economic growth. A particularly important event was the reprivatisation in 1991 of the banking sector, which had been nationalised in 1982.

"Since we did the pension reform more than 10 years ago, we have large local institutional holders which are pension funds, whose assets under management are currently close to $100 billion (this figure is compromised of fixed income and equity markets as well)," says SLT's source.

He adds that after the reforms of 2007, increased investment guidelines meant pension funds were turning away from 'traditional' opportunities such as securities lending. A move in 2005 by Banco de México to open up the local markets to foreign entities and to encourage mortgage companies to start lending gave the market a boost. However, this was stilted when ambiguities around tax regulations caused many of these new lenders to pull out of Mexico.

"Let's say that they [the pension funds] have a large proportion of the local government debt. What has happened is that even when we made the regulatory changes in 2007, we have been increasing the investment guidelines that they have, so instead of looking to more traditional opportunities, such as securities lending, they are looking more at starting an optimised exposure to foreign markets, or investing different products like equity, so the change has been quite important, and securities lending has not been the priority."

However, the clouds have been lifted somewhat by the changing sentiment around short-term returns and their importance. Says SLT's source: "At one point, pension funds were so concerned with short term profits that they were not lending their securities to banks because they didn't feel comfortable. Now that the pension regulator has been making changes to implement longer-term practices, things are set to change."

Recent reforms have been less drastic, but still hopeful of marching the market forwards. In March 2011, Consar, the Mexican pensions regulator, issued a directive that allows pension schemes (Afores) to employ external managers to look after a portion of their assets. This came as good news for the asset management industry, considering that Mexican pension funds have now roughly $120bn of assets under management, corresponding to 10 percent of Mexico's gross domestic product. "It is a positive development for the system, because it will allow workers' funds to be invested in a better way and be in a better position to take advantage of the current limitations to investments," says Isaac Volin, country head for Mexico at BlackRock.

SLT's source adds that the Banco de México has also been making some changes to the market makers programme with the Ministry of Finance. "In the past, you could obtain any securities on loan—with certain limits—and the cost for these securities was standardised, and there were no specials in the market. Whatever you were requesting, you would pay the same fee. Two or 3 years ago we changed that. If you are a market maker and you can demonstrate that you are conducting securities lending outside of this particular window of the programme, you will have a reduction in the cost you have to pay to the central bank.

So the idea is to incentivise market makers to trade outside of this facility, and if they start to borrow and lend securities that are not coming from the window of the Central Bank, they will have a reduction in cost. Today we have a somewhat spread-out cost structure. Over time hopefully it will be something we end up doing more."

Depositories

"We have two systems that can be used for securities lending. The central depositories system in Mexico is called Indeval, and that is owned by all commercial banks, and this depository was the first one to offer a system to trade securities lending. A few years ago Banamex, which is a subsidiary of Citigroup, developed their own system which is called Accival, to compete with which is a good sign because it means people are seeing value in securities lending," says SLT's source.

In 2009, Mexico's central securities depository launched Dali, a new securities settlement system, with the help of IBM.

Indeval's system, three years in the making, replaced more than a dozen prior settlement systems. The move also allowed to switch from a Model I settlement system, where securities and cash positions are settled on a trade-by-trade basis, to a Model III system, where cash and securities positions for many trades are netted at the end of a settlement cycle.

"There can be many such cycles in a trading day; and such continuous netting can happen nearly in real time, using IBM's Ilog CPlex optimisation software which matches thousands of transactions simultaneously," explains international editor at Securities Technology Monitor, Chris Kentouris.

The benefits are potential savings of $240 million in potential interest fees, which is the estimate of Mexico's central bank for more than 100 financial institutions using Indeval over the past eighteen months.

In a case study issued by IBM in December 2010, Indeval's chief executive Hector Anaya was cited as praising the new settlement system. He said: "It holds the unique distinction of being the world's only securities depository to have achieved near-real-time settlement in a Model III process. It will certainly be applied broadly by other central securities depositories, including corporations as they become aware of our success."

Collateral types

In Mexico, eligible collateral is set out by the Mexican authorities. While corporate bonds are still being accepted, the global financial crisis has highlighted that these bonds have lower liquidity than federal bonds. Therefore, the acceptance of corporate bonds depends on their own liquidity ratios and credit worthiness.

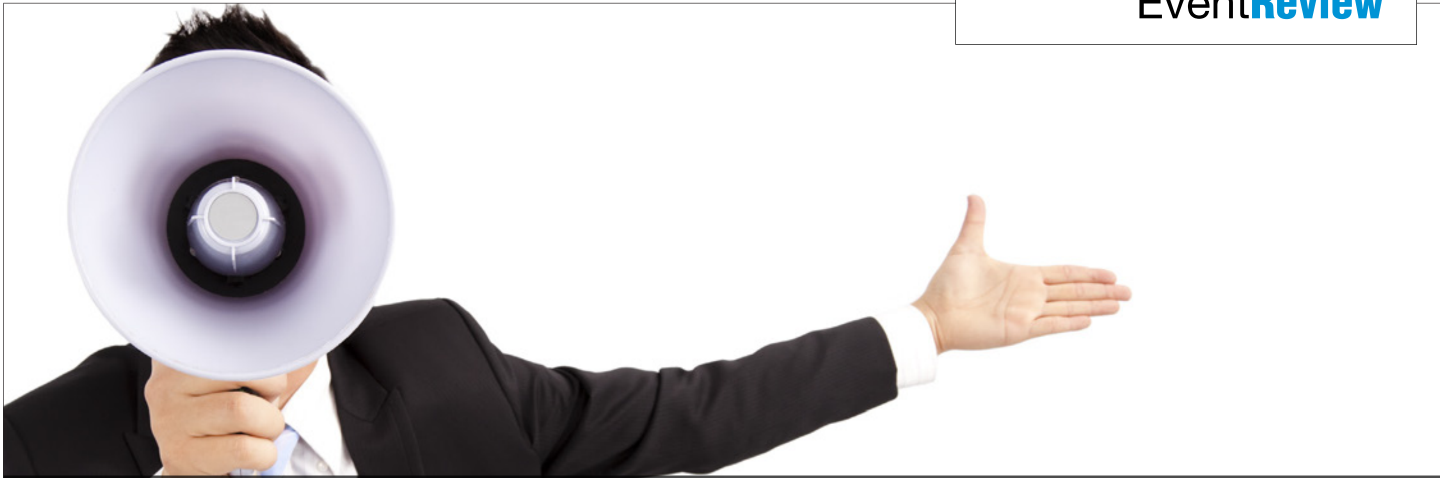
Typically, federal bonds have far higher levels of acceptance in regards to collateral. And in spite of the advantages of cash, for example, no haircuts or interest accrual, the current rules and regulations do not include accepting cash as collateral.

In addition, people are becoming far more cautious in terms of the types of collateral they accept. Locally, clients lending securities are being more careful about the collateral they will accept; they usually ask for government bonds or liquid shares, when in the past, they were more open to receive mutual fund shares.

"We have a pretty particular fixed income market in Mexico," said SLT's source. "We are different from other markets, most particularly the US market, which has a broad range. In our local market, most transactions are collateralised with government debt."

Manuel Torres Barajas, the executive director of treasury and short term interest rates for BBVA Bancomer, Mexico, notes that the volume of securities lending transactions has decreased from 2009-2011. "Securities lending was of course affected by the global crisis, which led to a loss of participation of many market makers. Before this, the daily average was MXN50 billion, compared to MXN35 billion, at which it currently stands."

"There's been some efforts from the Ministry of Finance, from the Central Bank, and the pension fund regulator to try and promote the use of securities lending amongst investors," concludes SLT's source. "So far, we have not been successful. If you look to a number of transactions made among private institutions, it is still quite low. Some of the pension funds have started to use securities lending, but its taking time—much more time than we thought when we published the regulation in 2007." **SLT**



When the conference calls: sec lending industry assembles

Will Duff Gordon of Data Explorers reports on the Securities Financing Forum in New York—Markit's first as the new owner of Data Explorers

DATA FORUM

Super panel

It is beyond doubt that low interest rates and few 'specials' (Facebook aside!) are causing market players to spend more time than ever negotiating the borrow/loan fee for in demand names. Eighty percent of the audience confirmed this in a vote. With this in mind, we gathered together representatives of all the key players in the securities lending continuum to see who was blaming who for this situation. Furthermore, we wanted to know what could be done to ease things.

On this topic, the custodian view was that borrowers had to bear in mind that the costs of being in business were rising across the board, leading to inevitable loan fee inflation. This is in addition to a lack of cash reinvestment revenue causing lenders to have to focus on the intrinsic lending fee. The hedge fund representative told the audience that it would be helpful for lenders to set their price according to the type of short sale that was behind it. The duration of the trade and the reason behind it will tell you how much the client will be prepared to pay.

I put our custodian on the spot to see if his desk is making efforts to do this. It sounds like they are trying to take this into account where possible, but the scale of business they are running makes it challenging. This panel, and audience voting results throughout the day, showed that the buy side can put up with high borrowing costs, but it is the fluctuation that they do not like.

There was no strong view on the panel as to which player is setting the agenda at present. Conversely, the audience seemed adamant with 42 percent thinking that beneficial owners are in command. Our prime broker representative rightly said that regulators are the pacemaker of today's markets. Anthony Nazzaro, who advises the conservative-minded beneficial owners, said it certainly wasn't this type of asset owner who is agenda-setting. But he could see huge opportunity and power with the larger and more sophisticated beneficial owners who were able to entertain the types of trades that are in vogue, such as term lending and collateral transformation. Our custodian agreed that those of his clients who were flexible enough to change guidelines to suit the times were those who could both earn the most and could set their own terms. In this environment, securities lending is certainly not for everyone, he said.

There was a good discussion about whether the chain remains too long given that most other markets have moved to central clearing or trade repositories. Espousing a Darwin-esque line, the agent lender pointed to the chain surviving the test of time. It remained intact for a reason. The buy-side member of the panel was of the view that in uncertain times there is safety in doing business in the way one always has. There is comfort in having lots of players in the chain with so much credit, market and regulatory risk.

Muted hedge fund demand

With low interest rates, advancing tax harmonisation and regulatory changes, the securities lending industry is more reliant than ever on hedge funds to drive borrowing demand. But market volatility has thrown the traditional drivers of borrowing away from the markets. The strategies that use the most leverage are dong the worst this year, especially macro and convert arb. One panellist noted that our investors don't want a levered up factor quant model, appealing for better rates for longer fixed periods to stimulate borrow demand. Yet other panellists argued the market should take more leverage, if it is on offer.

The confusion over regulation was equated to a slow and painful death, unlike Lehman Brothers, which offered the mercy of a quick kill. We heard that quant macro is very hard at present—the future not based on the past! But a prime broker accused the buy side of a lack of conviction and noted that hedge funds were less aggressive. On a more positive note, we heard that last month the long/short strategy has come into its own.

How to increase revenues?

The harsh reality of recent years is set to continue for the foreseeable future, but this panel was focused on opportunities. The debate between synthetic and physical prime brokers is one example where switching between the two can result in great benefits. Clearly, some transactions work better with synthetics and marrying customer needs alongside optimising returns is important. It will be the clients, asset and strategy that determine the route of borrow. However, one panellist noted this was a race to the bottom.

Single stock futures are another bright spot—backed by OCC, the panel argued that they are a good alternative for swaps and help with yield optimisation, cash management and equity finance, with no collateral management worries.

Concerns were raised that the pricing of collateral transformation and term lending is not attractive enough from a beneficial owners perspective, with data showing hedge fund term becoming shorter yet bank term getting longer. This will cost banks money, which will be passed on to their beneficial owners and hedge funds in terms of pricing.

Training and Education

18-19 June	London	**Operational Risk Management** This two-day practical course explores the best practice in operational risk management, at all stages, from assessment to implementation. You will gain tools to manage risk and to create environment where this function is perceived as a value added proposition increasing profitability and structural strength of an orgnisation.	Eureka Financial
18-19 June	London	**Syndicated Lending and Documentation** This two-day course will provide delegates with a detailed understanding of the syndicated loan product, its uses and market practices.	Marcus Evans
21 June	London	**The Repo Market** This 1 day course is designed for delegates who are new to the business of bond repurchase agreements (repos) and aims to explain how repos are priced, settled and why they are transacted by different participants in the market, including pension funds, hedge funds, market makers and derivatives users.	Eureka Financial
28-29 June	Hong Kong	**Repos and Securities Lending** Repos and Securities Lending provides a comprehensive and practical programme explaining the legal, regulatory and documentary issues involved in repo and securities lending transactions.	Euromoney Training

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Industry appointments

Richard Marquis, formerly of J.P. Morgan, will join BNY Mellon, according to an SLT source.

Marquis was an executive director in the securities lending and equity financing group within J.P. Morgan's prime brokerage business.

SLT has been told that Marquis will work in BNY Mellon's equity lending business and will report to Robert Chiuch, who is a managing director in its securities lending business and leads the US equity and corporate securities lending team.

SLT understands Marquis will continue to be based in New York.

Euroclear's **Marc Antoine Autheman** will succeed **Nigel Wicks** when he retires as chairman of both the Euroclear plc and Euroclear SA/NV Boards on 1 January 2013.

Autheman will become deputy chairman of both Euroclear boards immediately, a position that he shares with Jean-Jacques Verdickt.

Rockall Technologies, a solutions provider for collateral management, will see **Avi Gur** join the company to further enhance its expertise in the structured trade and commodity finance (STCF) business.

Gur will be based in London, which is a first step to Rockall establishing a physical presence there.

Southwest Securities, the commercial banking subsidiary of SWS Group, has named **Eddie Gutierrez** as president of the company's banking center in Albuquerque, New Mexico.

"Eddie Gutierrez is well known throughout Albuquerque and the surrounding area as a respected leader in the commercial banking industry with a special expertise in SBA lending," said Robert Chereck, executive chairman and president of Southwest Securities.

SWS Group is a Dallas-based company. Its subsidiaries include Southwest Securities, a national clearing firm, registered investment adviser and registered broker-dealer.

Interdealer broker ICAP has appointed **Andy Coyne** as the new CEO of Traiana, its post-trade technology division.

Coyne joins Traiana from Citi, where he was head of FX prime and eCommerce products. He will be based in London and report to the founder of Traiana, Gil Mandelzis, who has moved to the newly created role of executive chairman.

Masamichi Kono is to be the new chairman of the International Organization of Securities Commissions (IOSCO) board.

Kono indicated he would step down from the position in March 2013, with Greg Medcraft, the chairman of the Australian Securities & Investment Commission (ASIC), taking over until he too steps down at the IOSCO annual conference in September 2014 in Rio de Janeiro.

The board also appointed two vice chairs: Vedat Akgiray, the chairman of the capital markets board of Turkey, and Ethiopis Tafara, the director of the Office of International Affairs at the US SEC.

ABN Amro Bank's heads of equity finance and information technology solutions, **Sander Baauw** and **Raymond Vuyst**, have joined the IT company Synechron.

Baauw and Vuyst have become managing directors at Synechron. They moved on 1 May and are based in Amsterdam.

Baauw spent 11 years at Fortis Bank, which later became ABN Amro. He was responsible for equity finance trading in Europe.

Vuyst was in charge of IT solutions for the securities financing and the equities derivative departments at the bank.

"On the IT side we were always hiring Synechron for implementation, interfacing, testing, monitoring 24/7 and software development. That's how we came to know them and move there," said Baauw in a telephone interview.

Synechron provides IT services to the banking, financial services and insurance industries, as well as to digital media and technology companies.

Baauw added: "We are going to focus on capital markets at Synechron. "

"But what we're focusing on in the first instance is securities finance. At this moment I don't see a dedicated IT company in the securities finance business like Synechron."

Global head of prime brokerage sales at BNP Paribas, **Samuel Hocking**, has left the bank.

Formerly working in the prime brokerage division of Bank of America, Hocking resigned for personal reasons, and stated he intends to take the summer off. **SLT**

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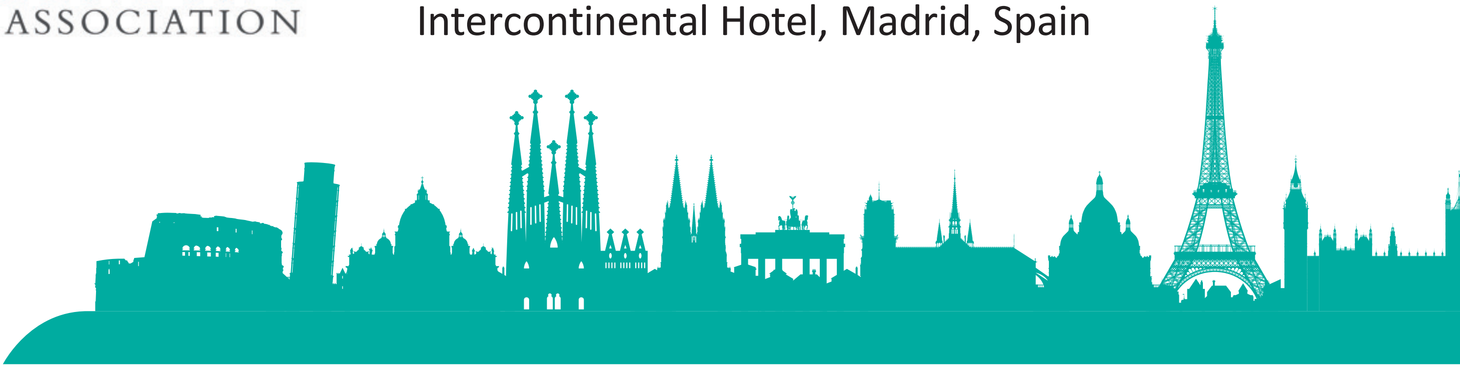

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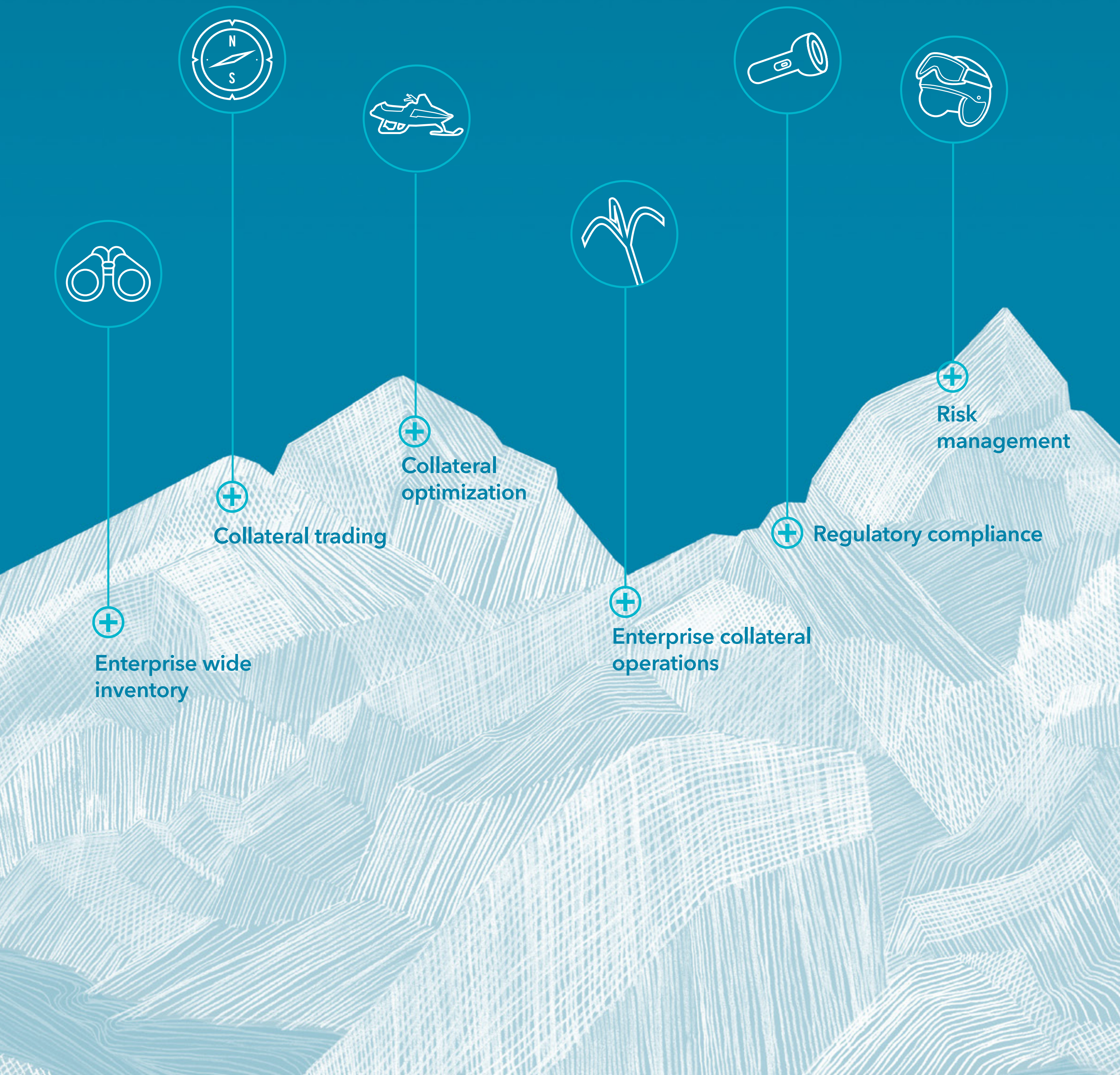

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