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Eurex to launch Europe's first securities lending CCP service

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Eurex Clearing will soon launch Europe's first central counterparty (CCP) service for the bilateral securities lending market in partnership with Pirum Systems and Clearstream Banking.

It plans to launch the new CCP on 22 November. "This offering will be the first service in Europe to preserve the special structure of the securities lending market combined with a proven and industry-accepted CCP model that provides transparent and standardised risk management and robust default procedures," said Thomas Wißbach, senior vice president at Eurex Clearing.

Eurex is the first clearinghouse to integrate the securities lending market model into an industry-accepted CCP model, which allows cash and non-cash collateral, and provides automated trade flow and loan lifecycle management.

Wißbach said that over the past two years, Eurex has held extensive consultation sessions and working groups, leading to many interested borrowers and lenders from a wide geographical area committing to the service.

He added that agent lenders that have been involved in the consultation phase of the service from the start have been "very supportive, in particular, [of] the ability to maintain their existing bilateral trading relationships—an opportunity to increase their range of borrowing counterparties".

"They have also welcomed our innovative specific lender licence that enables their beneficial owners to participate in the service without paying margin for their securities lending transactions," added Wißbach.

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SLTINBRIEF

Citi and UBS offer joint post-trade solution in APAC

Citi and UBS have launched a combined service offering that provides a post-trade solution to broker-dealers in Asia Pacific.

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Greece extends short selling ban

The Hellenic Capital Market Commission (HCMC) has decided to extend a ban on short selling for three months, effective from 1 November.

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Eurex to launch Europe's first securities lending CCP service

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The new CCP will commence operations with an initial group of banks and asset classes, starting with German and Swiss blue chip equities and exchange traded funds.

With customers set to go live on the service this year, Wißbach added that "many others are planning their integration to the service in the first half of 2013 when the service will be extended to include fixed-income securities and further European equity markets."

It will combine the trading capabilities of Eurex Repo's SecLend Market and Pirum's Real-Time service, with the triparty collateral management services of Clearstream Banking Luxembourg and Euroclear Bank. The new offering also meets regulatory requirements including, Basel III and IOSCO proposals.

Thomas Book, member of the Eurex executive board and responsible for clearing, said: "Our new clearing offering for securities lending has been designed with support from key market participants who have committed to utilising the service to achieve a substantial reduction in capital allocation. We have completed testing of our offering and are ready to start a pilot phase with our early adopters."

"Our set-up will enable customers to make use of their existing connectivity to these dynamic service providers for trade and collateral management and to take the benefit of substantial improvements to the current market structure by delivering significant capital and operational benefits to all participants," added Book.

Citi and UBS offer joint post-trade solution in APAC

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The joint solution will provide middle office, back office, clearing, asset servicing and custody capabilities to broker-dealers that are seeking to minimise cost, while retaining operational flexibility.

Andrew Murfin, regional head of UBS's group operations, said: "Firms are increasingly having to review their operating options given the extreme pressure on cost bases and a regulatory environment that is highly challenging and rapidly evolving."

"UBS believes that this will drive a preference for buying expertise to service business rather than developing processes and technology in-house which require significant investment and lead to an unsustainable level of fixed costs," added Murfin.

David Russell, regional head for Asia Pacific securities and fund services at Citi, said: "Citi is pleased to be working with UBS on this market-leading solution for the region. The collaboration reinforces our commitment to our clients, by working with select partners to build operational infrastructures to better serve market participants."

Greece extends short selling ban

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The additional three-month ban is an extension of the HCMC's previous ban—which it introduced in August—that expired on 31 October.

The European Securities and Markets Authority (ESMA) released its opinion on Greece's ban extension on 1 November.

"ESMA considers that there are adverse developments which constitute a serious threat to financial stability and to the market confidence in Greece."

"ESMA [also] considers that the duration of the measure is justified and appreciates the HCMC's statement in its notification of intent whereby the measure may be lifted during the period of enforcement of the measure, if considered necessary," said a statement from ESMA.

Spanish regulator the CNMV also extended its short selling ban for a further three months from 1 November. The ban is an extension of a seven-day ban that it introduced on 23 July.

The EU Regulation on Short Selling and Aspects of Credit Default Swaps came into effect on 1 November.

ESMA recently released a question and answer document to help authorities, investors and other market participants better understand the new European short selling regulatory regime.

The document provides responses to questions posed by the industry and offers clarity on the requirements that were introduced under the short selling framework.

Subjects covered in the paper include transparency and calculating of net short positions, uncovering short sales and enforcement of the regulation itself.

The document will be continually updated as new queries arise.

"The objectives of this short selling legislative framework are to increase transparency of short positions held by investors in certain EU securities, reduce settlement and other risks linked with uncovered or naked short selling and create a harmonised framework for coordinated action at European level," stated the ESMA document.

OCC's securities lending activity up 31 percent

Options Clearing Corporation's (OCC) securities lending CCP activities saw a 31 percent increase in new loans from October 2011 with 77,292 transactions in October.

Year-to-date stock loan activity is also up 26 percent from 2011 with 813,950 new loan transactions in 2012.

Futures cleared by OCC reached 3,247,032 contracts in October this year, a 31 percent increase from October 2011. Equities futures reached 424,573 contracts this month, up 149 percent from 2011.

Average daily options trading volume in October was 15,444,282 contracts, which was 17 percent lower than October 2011. Total options trading volume for the month reached 324,329,913 contracts, also a 17 percent decline from October 2011.

OCC's year-to-date options trading volume is down 14 percent with 3,355,815,364 contracts.

OneChicago volume is on the up

OneChicago has announced its trading volume for October 2012, revealing that volume of 424,573 was up 149 percent over October 2011.

Other October highlights included 412,066 exchange futures for physicals (EPFs) blocks traded, with EPFs and blocks activity representing $1.9 billion in notional value.

OneChicago's equity finance tool—OCX.NoDIvRisk—which removes dividend risk for clients carrying equity delta exposure, accounted for 48 percent of October 2012 month-end open interest.

Open interest stood at 487,155 contracts on the equity finance exchange at the end of October 2012, which was up 31 percent year-on-year compared with October 2011.

Swiss Life Asset Management selects SGSS

Swiss Life Asset Management has chosen Societe Generale Securities Services (SGSS) to provide securities services for 60 investment funds totaling €5.5 billion of AUM.

SGSS will provide the French UCITS with fund administration and securities lending services, and it will provide the Luxembourg UCITS with domiciliation, custody, fund administration and securities lending services.

J.P. Morgan offers daily portfolio reconciliation

J.P. Morgan's Agency Clearing, Collateral Management and Execution (ACCE) business has

introduced daily portfolio reconciliation for its derivatives collateral management clients.

The product, which is available through ACCE's TriOptima partnership, enables clients to use secure FTP technology and exchange trade files through the triResolve service.

John Rivett, global collateral management business executive for ACCE at J.P. Morgan, said: "Daily portfolio reconciliation minimises delays in identifying valuation differences, trade booking errors and other potential discrepancies. This lessens the likelihood of disputes and helps clients accelerate the resolution of any potential queries."

FINRA approves Cowen's KDC Securities acquisition

A source has confirmed that the US Financial Industry Regulatory Authority (FINRA) has approved Cowen Group's purchase of KDC Securities from Kellner Capital.

KDC Securities is the New York-based, securities lending business and broker-dealer subsidiary of hedge fund manager Kellner Capital.

Formerly called Kellner DiLeo & Company, the hedge fund manager rebranded in May euroclear

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The right securities – at the right place – at the right time as Kellner Capital and launched a new event-driven investment fund with more than $50 million in assets.

Kellner Capital agreed to sell KDC Securities to Cowen Group, which provides alternative investment management, investment banking, research, and sales and trading services through two business segments, at the end of September.

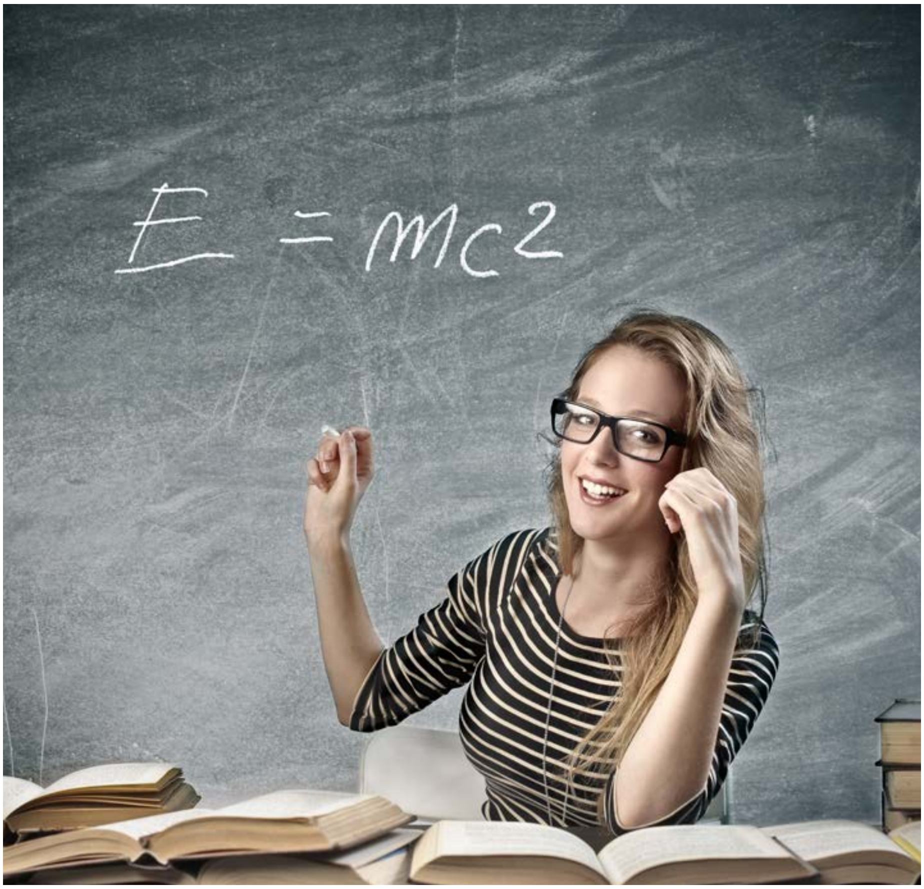
Ramius and its affiliates make up Cowen Group's alternative investment management business, while Cowen and Company is its broker-dealer.

The broker-dealer offers industry-focused investment banking for growth-oriented companies, domain knowledge-driven research, and a sales and trading platform for institutional investors.

KDC Securities will be rebranded as Cowen Equity Finance Group. It will continue to be based in New York.

Rory Zirpolo, the head of securities lending at KDC Securities, will serve as managing director and head of the equity finance group. He will report to Cowen Group's co-heads of equities, Tom O'Mara and Dan Charney.

Joining Zirpolo at Cowen Group are Barry Skarbek, Jill Mandarino, Stephen Grazioli and Richard DePaulis.



Speaking at the time that the deal was announced, Jeff Solomon, CEO of Cowen and Company, said: "Kellner [Capital] and its securities lending team have built an impressive equity finance platform since the business was launched seven years ago. We believe the business is well positioned for future growth and is a strong complement to our existing sales and trading footprint."

Zirpolo previously worked as managing director of prime services at Credit Suisse, where he was responsible for a $50 billion supply side securities lending business, before joining what was then Kellner DiLeo & Company in late 2010.

As a part of his role at Kellner Capital, Zirpolo works as the portfolio manager of KDC Alpha, a matched book securities lending portfolio.

Collateral quality equal to cost

Almost all of the respondents to a Six Securities Services survey believe that the quality and cost of collateral should be given equal consideration.

Whilst 92 percent of participants consider the quality of collateral to be as important as the cost, 85 percent of respondents believe that selecting a market infrastructure on cost alone increases exposure to risk.

The data released from a micro-survey conducted at the Sibos conference in Osaka, Japan, recorded the opinions of sell-side banks and broker-dealers relating to collateral and the safety of market infrastructures.

Commenting on the results, Thomas Zeeb, CEO of Six Securities Services, said: "Some CCPs (central counterparties) believe that generating new collateral by securitising and repackaging existing portfolios is a way forward. I fundamentally disagree with this approach."

"That the industry is already thinking about repeating the sins of the past, by repackaging securities to create new collateral pools is

frightening. Collateral should be simple, of high quality, liquid, and easily-valued. Competing on poor collateral quality sows the seeds for the next failure and subsequent crisis."

Focusing on the amount of collateral available, 69 percent of respondents believe that there is enough collateral to go around.

"The opinions of the largest sell-side banks is that there is enough collateral in the system, but due to regulatory requirements, the liquidity is not being distributed efficiently," said a statement from Six Securities Services.

"Collateral management and its optimisation are major concerns for financial institutions at the moment. Collateral is not being distributed efficiently," concluded Zeeb.

4sight releases new collateral optimisation white paper

Software solutions provider 4sight Financial Software has published a new white paper on collateral optimisation.

The new paper covers what collateral optimisation is and what is driving it. The paper also provides techniques that can be used by firms to optimise their collateral, and how these techniques are helping firms to adapt to regulatory change.

Martin Seagroatt, 4sight's head of marketing, said: "Collateral optimisation is currently one of the most talked about subjects in the financial world due to new regulations such as Dodd-Frank, EMIR and Basel III."

"The paper aims to provide some clarity on how financial firms of all sizes can respond to an environment where quality collateral is in short supply and looks at how optimisation may develop in the future."

OneChicago marks OCX.NoDivRisk's birthday

OneChicago has celebrated the second-year anniversary of its exchange-traded equity finance product, OCX.NoDivRisk.

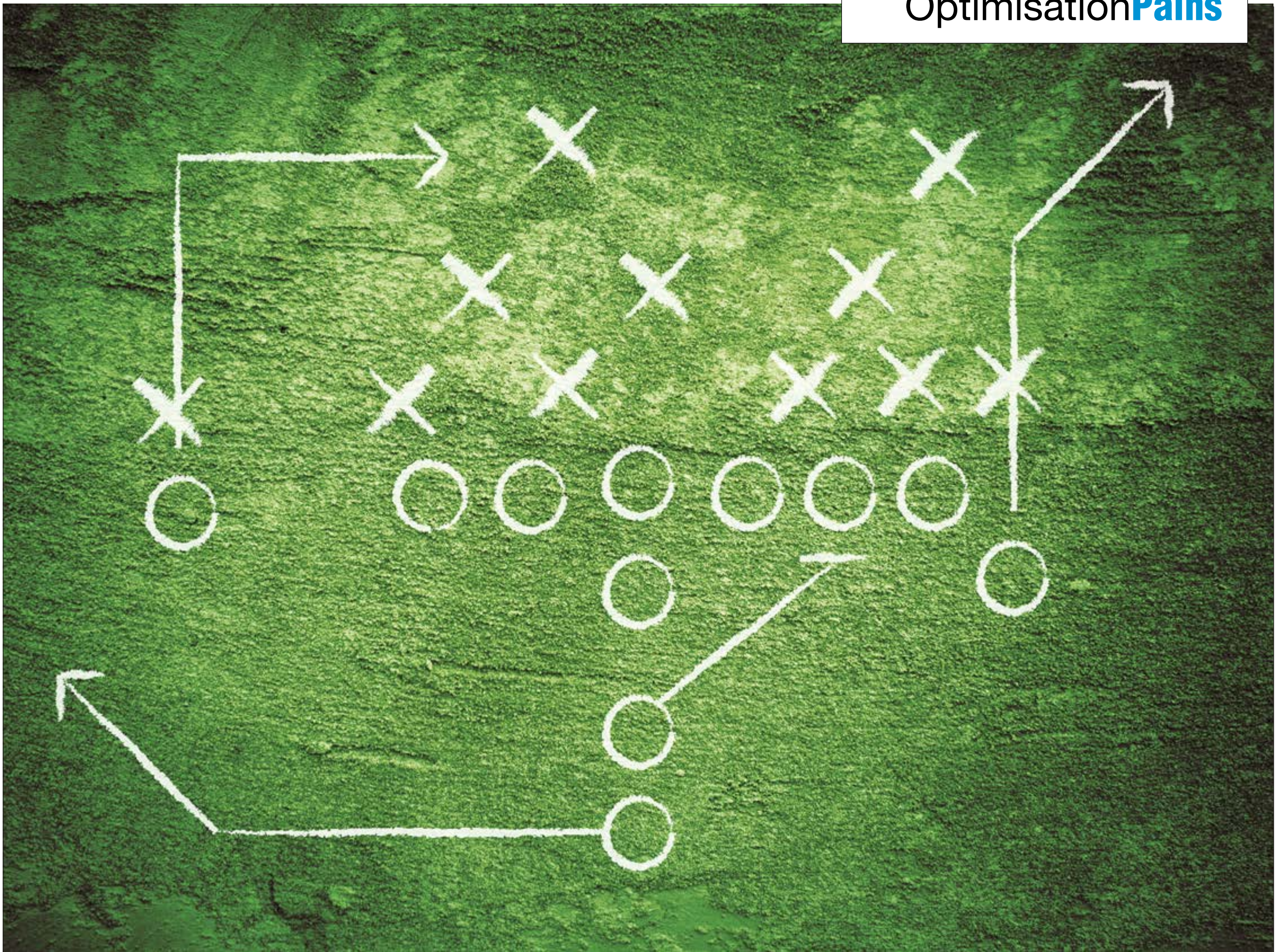
OCX.NoDivRisk allows traders to hold equity exposure without dividend variation risk. Since its launch in Q4 2010, the product has grown to 59 percent of the exchange future for physical (EFP) volume, 44 percent of the block volume and 46 percent of the open interest.

David Downey, CEO of OneChicago, said: "The dividend risk is removed as we adjust the OCX.NoDivRisk contract's prior night's settlement on the morning of ex-date by the then known actual dividend amount. This adjustment is done without any pay/collect cycle between the long and short parties. Removing the dividend risk allows market participants to trade without worry of how dividend changes could affect their holdings."

OCX.NoDivRisk can help firms to address upcoming regulations such as the US Dodd-Frank Act and Basel III.

An EFP transaction using the OCX.NoDivRisk contract is a pure interest rate trade that is equivalent to an OTC equity swap such as an equity repo or stock lending transaction, which are "the very transactions that Dodd-Frank envisions moving to exchanges and clearinghouses", said OneChicago in a statement.

"Firms looking to trade on better financing and leverage terms with an upgrade of their counterparty exposure to a AA+ entity, the OCC, and those entities that will soon to be affected by pending Basel III capital constraints will find the products attractive."



Catch collateral if you plan

SLT talks to David Field of Rule Financial about the work that financial institutions still have to do to lighten the collateral load

JENNA JONES REPORTS

In what ways has collateral management changed in the previous few years?

The biggest change is that collateral management is now centre-stage, whereas before it was very much a back-office function. It used to be considered as not very important, but in the last two years it has really come to the forefront. A firm's complete focus used to be on trading systems. Now, collateral trading and the collateral function have become the main focus.

The changes in collateral management are driven by the advent of a new regulatory regime. The two key regulations are the US Dodd-Frank Act and the European Market Infrastructure Regulation (EMIR), and both of them require OTC derivatives to be centrally cleared, with the clearing houses demanding collateral to hold in order to do so. This regulatory change was driven by the G20 countries, which expressed their opinions on the importance of clearing and collectively agreed to enforce it. Firms now realise that they have a considerable amount of collateral to find, collateral that they do not currently have, and this has become a major problem for them.

How could a shortage of collateral affect particular businesses such as repo and securities lending, and how can they overcome shortages?

There have been numerous estimates of the shortfall of high quality collateral across the market. Some of these estimates place the shortfall as high as $6 trillion. The Bank of England recently published its collateral demand model for swaps and credit default swaps, which indicates that around £0.5 trillion (approximately $800 billion) of additional collateral will be required. But that figure itself assumes normal market conditions. In volatile conditions, such as those that we saw in 2007 to 2008, central counterparties (CCPs) and others start calling for a much greater margin, and in those circumstances the extra collateral needed across the industry could be as high as $2.6 trillion.

In practice, no one knows how much more collateral will be needed, but I believe we can be fairly confident that the shortage may actually be in the trillions and not billions.

We think that this means the repo market will become much more proactive, as many more securities have the opportunity to become 'special' (meaning that there is specific short-term demand for them), enabling the repo trader to make more money from them. At the same time the market is also likely to become more stratified. Instead of an issue being either 'special', or 'not special', we think that there will be a more refined set of grades. Potentially, an issue may be defined as 'a bit special' or a 'bit more special', and as a result the market will become much more sensitive to the value of collateral.

For OTC markets, the cost of collateral will have to be factored in to the price of the deal. In other words, collateral pricing will need to be available pre-trade in the front office, meaning that market participants must make maximum use of the resources that are available to them. Not surprisingly, we are seeing most firms initiating some kind of collateral optimisation initiative. This has major implications for their operating models, and of course requires strong technology support.

How are firms that act across multiple product lines integrating collateral management into their operations?

Collateral management is already integrated into firms operations, but it's not integrated across their operations, so most firms operate in silos. Silos are often organised by asset class, so in each area where you have a trading system, there will be a back-office operation system with a collateral function, often in a silo all of its own. For example, the futures business, the repo business and the prime brokerage business will all contain collateral, but they are not integrated. So you may have bonds in one, equities in another and cash in all three, but with no single view.

We see many initiatives being created to enable a single stock record, either physically or virtually. With this in place, firms should at least be able to see an integrated view of all their collateral, even if it's not located in one place. If collateral in a firm is held in different places, and the newly formed central collateral function built around the prime brokerage unit can't see the collateral executions, or what's in New York or Singapore, then how can it possibly optimise its collateral?

What do you advise clients if they are unable to optimise their collateral due to geographical disparity?

We wish them luck! In practice though, they don't really have a choice, unless they happen to have so much collateral that it doesn't really matter. They have to come up with a business operating model that allows collateral to be used in the right place, in the right time zone, and be allocated against the right liabilities or risks. And this allocation has to take into account all of the eligibility, haircuts and fee structures that will vary by venue. Collateral re-allocation has to be enabled in the operating model, in a highly efficient 'follow-the-sun' (if necessary) STP environment, with all the right profit and loss allocations in the right jurisdictions. There are also many constraints about what collateral can be moved between jurisdictions, so there are limits to how much optimisation can actually be achieved across geographies.

How is technological innovation shaping collateral management?

Technology vendors have certainly realised that this is a big opportunity. Some vendors began investing in product enhancements two or three years ago to accommodate collateral management. They started building much more sophisticated collateral management platforms that provide functionality such as: single stock record, sophisticated collateral management and collateral optimisation algorithms. These vendors are now reaping the rewards and winning competitive tenders from banks and CCPs.

Other vendors, some of whom have historically enjoyed significant market share in repo or stock borrow and lend, have been slower off the mark and are running the risk of losing market share and being left behind. But changing an enterprise collateral management system is not for the faint-hearted, it's potentially a massive job. However, with very limited options, we are right now seeing many firms having to grasp the nettle and consider re-platforming.

But innovation is not restricted to the package vendors. For the last two years, the tier one banks have been spending $50 million or so a year on technology innovation to deliver the same business functions, but more usually on systems developed in-house. Because they started early, they have the foundations in place and are now well positioned to lead the market and retain their dominance. The second tier firms are struggling to catch up, and are often constrained to doing the minimum that is necessary to protect their customer franchise.

How are regulatory changes driving the need for technological solutions to collateral management problems?

The regulations have set out very specific requirements to be met by specific dates. For example, under Dodd-Frank and EMIR, customers will have a choice about whether they are happy for their collateral to be held in an omnibus account, which is cheaper to operate, or to be fully segregated, which is safer but more expensive.

If many large account managers opt for full segregation, the industry will have a major challenge in dealing with a proliferation of accounts that have to be mirrored through the broker, the CCP and the triparty agent. This can only be achieved by putting the right technology in place.

Are there any technological advances that you would like to see happening for your clients, but aren't?

The issue is not lack of technological advance, but lack of take-up of the technology that is already available. There are plenty of advanced solutions that are available which cover most, if not all of the componentry that firms need in the new world of clearing and collateral.

There are three main constraints that have held back technology adoption. First is the huge expense that is involved in introducing a new collateral platform that touches so many parts of the bank's infrastructure, plus the significant integration and testing costs. A second inhibitor has been uncertainty about the regulatory requirements. It is not uncommon for firms to hold back on investment until they are more confident that the regulations will actually be implemented, and indeed whether the initial dates will slip. Finally, many have held back because some of the detail is still not pinned down; however, this is no longer a valid excuse. These regulations will happen, and though the dates and details may change a little, enough is now known for projects to start. Anybody still holding back on these grounds will almost certainly miss the boat.

Unfortunately, there may also be a fourth emerging constraint on technology adoption: a lack of resources on the supply side. Customers are already signing contracts with vendors with good solutions, and vendors are allocating their 'A teams' to these prestigious projects. These projects are strategic to both the vendor and the buyer, but there are only so many 'A teams' to go around. Firms that are late to the party will still demand the vendor's top team, but they simply won't be available. We are already seeing some vendors being quite careful about what new opportunities they are willing to bid for.

In summary, by now firms should be designing their new business operating models and their target technology architectures, and they need a reasonably well-defined implementation roadmap, at least for 2013. As investment budgets are formed up and we enter the next financial year, execution projects need to be mobilised pretty quickly if firms are to deliver the technology that they will need to have in place during the course of 2013. **SLT**

David Field
Specialist in clearing and collateral management
Rule Financial

Nordic lights

SLT's experts look at the securities borrowing and lending market in the Nordic region and find that it is doing well despite wider European woes

David Lewis
Senior vice president, Astec Analytics
SunGard's capital markets business

Dag Rudiløkken
Head of trading, securities finance
DNB Bank

John Irwin
Head of international trading
Northern Trust

Jakob Burell
Head of equity finance
SEB

How would you describe the state of the Nordic securities borrowing and lending market?

Dag Rudiløkken: The Nordic securities borrowing and lending market was heavily hit by the financial crises like the rest of the world. The market has slowly been recovering but is still far from the volumes that we saw prior to 2008 and 2009. Most lenders have or are planning to return to the market, but we see that many of our borrowing clients have both reduced ability and willingness to take positions in a market with as much uncertainty as we see today.

Jakob Burell: It has been fairly healthy throughout the last couple of years. Volumes have absolutley decreased in the equity space, but not as much as anticipated. The Nordic region has not suffered as much from the financial crisis as one would expect. That has led to quite a lot of overseas investments due to the perception of low risk. In combination with a transparent equity market and an efficient stock lending market, the Nordic region is pretty well positioned.

Lewis: As a collective group, the Nordic countries do not all face the same regulatory issues as each other, or the wider international market

David Lewis: The Nordic market is in many ways a separate market area in its own right, which is not untypical of such a region where the constituents are so closely bonded together. This co-dependency has no doubt helped keep the market buoyant during the recent crisis.

What trends and developments have you observed this year?

John Irwin: The Nordic region has weathered the effects of the global financial crisis better than most. Sweden, Norway, Finland and Denmark have all preserved their Triple AAA credit ratings that were assigned by both Moody's and Standard & Poor's, and none have faced the liquidity challenges that have affected many other parts of Europe. As a result, many of the themes that have been the catalyst for securities lending demand in other parts of Europe have not be as prevalent within the Nordic region. The relative strength of the region's banking sector has meant that we have not seen the wide scale capital raising (ie, rights issues, convertible bond issuance) that has been endemic in other pockets of Europe across this sector. The level of corporate activity (M&As and IPO issuance) in the region over the last 12 months has also been relatively modest as well.

Overall, higher intrinsic value lending opportunities have been relatively modest and typically centred around specific long-term, fundamental-based long / short strategies in isolated sectors. For example, a slowing Chinese economy continues to present challenges for pockets of the raw materials / oil and gas exploration securities that have been the focus of borrower demand.

Rudiløkken: We have seen more activity than the previous two years. We have seen more demand for cash trades, and there has been more focus on what type of collateral we can give or take.

Burell: Quality / elegible collateral is what everybody is looking at from a market perspective. This is more a prerequisite to be able to facilitate for the clients and their demands. If one wants to keep the business, you have to make sure that you adapt to the new environment.

From a development perspective, it is all about automation and to streamline processes. Of course, it is also to meet the external demands coming from regulatory changes. Development is coming more from a defensive angle these days.

Does the Nordic market face the same regulatory burdens as the rest of the international market, and what are the key regulations taking up your time?

Lewis: As a collective group, the Nordic countries do not all face the same regulatory issues as each other, or the wider international market. While they do have some common rights and obligations, their membership of and involvement in the EU varies: Norway is not a member of the EU; Denmark, Sweden and Finland are; but Finland is the only Nordic country to adopt the euro. Denmark has felt both the positive and negative effects of its position of being both within the EU but outside of the euro. Seen as an effective hedge against euro exposure, Danish sovereign debt has been in high demand, so much so that the yields on certain maturities fell into the territory of negative rates. Denmark also supported a short selling ban on its financial shares. Although billed as temporary when instigated in 2008 to stabilise markets, this ban was only removed on 1 November 2012. This removal was timed to coincide with the arrival of the new European Securities and Markets Authority (ESMA) short selling regulations, which ban naked short selling and increase reporting requirements for given securities. These new rules will not, of course, affect all the countries in the Nordic region equally.

Burell: Swedish banks will have stricter rules on capital and the deadline for Basel implementation is earlier than the rest of Europe

Rudiløkken: We have more or less the same regulatory issues as the rest of Europe. Key issues are use / reuse of collateral, capital requirements and Basel III, along with the impact that this will have, both on securities-driven and cash-driven transactions.

Burell: Absolutely, and sometimes even more than others. Swedish banks will have stricter rules on capital and the deadline for Basel implementation is earlier than the rest of Europe.

The new short selling regulations are of course one of the obvious changes that we concentrate on—that is not affecting us as much as it affects our clients and their internal processes. We are a bit fortunate that we have worked with this alongside our clients for the last couple of years and they are quite used to the rules in their investment process.

The new disclosure rules are also something that takes up our time. Clients cannot afford

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to do it on their own so they outsource that to those who can be scalable like ourselves.

How well have automatic and opportunity borrowing and lending services fared over the past 12 months?

Rudiløkken: We have during this year seen an increase in volume and demand, both for automatic and opportunity borrowing and lending.

Irwin: Northern Trust is a founding member of EquiLend and has over a decade's worth of experience using automated pre- and post-trade functionality. We are an active user of EquiLend's suite of pre-trade 'Auto-Borrow' functionality and are EquiLend's biggest global use of EquiLend T20 functionality (a platform that matches lender supply and borrower demand).

We use EquiLend AutoBorrow across all active lending markets in the region (Norway, Sweden, Finland and Denmark) to increase utilisation of our client portfolios. We are also an active user of EquiLend's T20 platform that helps to support the utilisation of our clients' higher intrinsic value assets within their portfolios.

What are the average collateral requirements against market value of outstanding loans and how does this compare with the rest of Europe?

Burell: I would say that we are pretty aligned with the rest of Europe. In some areas, we are probably more conservative and in others we might be more flexible.

Irwin: Ongoing regulatory and funding cost sensitivities have meant that borrowing brokers are seeking to pledge a wider and more flexible range of collateral

Lewis: In the Nordic region, the principal lending model remains in place for many participants. It was not that long ago that collateral was not even posted between a beneficial owner and its principal borrower.

Rudiløkken: In Norway, we have a minimum collateral requirement of 105 percent that is stated in the regulatory framework. It is our understanding that this is the going haircut between most investment banks, but the haircut is significantly higher for other clients.

Up to now, the main collateral for securities borrowing and lending has been cash. We have, especially during the last year, seen that non-cash collateral has been requested by more and more counterparties and perhaps mostly by lenders that want to collateralise their lending in an efficient and secure way.

Irwin: Average collateral requirements across the Nordic region are largely in-line with the rest of Europe. However, as a general theme, ongoing regulatory and funding cost sensitivities have meant that borrowing brokers are seeking to pledge a wider and more flexible range of collateral (for example, equities and corporate bonds), especially when sourced readily available assets. Given the softness of the specials market within the Nordic region, clients with more flexible collateral guidelines have been better positioned to benefit from increased portfolio utilisation. Borrowers are often prepared to provide a higher level of margin to allow them the flexibility to pledge a broad range of the collateral.

How do you see the market looking in 2013?

Rudiløkken: It seems that the borrowing and lending market is in a positive trend and we think that this might be the picture in 2013 as well, but there are some uncertain factors that can change this—the financial recovery, especially euro stability programmes, but also the impact of regulatory burdens and Basel III.

Irwin: Looking forwards into 2013, expectations are that securities lending demand within the region will remain relatively stable. Hedge fund interest is expected to remain focused on the long / short directional strategies with most of the interest being focused on those sectors that have attracted demand over the past 12 months (for example, renewable energy, shipping and technology).

Over recent years, the Nordic region has suffered from its exposures to the Baltic States and its allying property sector. However, the regional economy has all but recovered and is now stabilising. From a corporate perspective, there is a general consensus that many companies are sitting with long cash on their balance sheets and at some point will need to put this capital to work. This should be the catalyst for an uptick in M&A activity within the region. However, in the absence of any clear indicators that the eurozone's issues have some definitive resolution, there is an expectation that any uptick will be modest.

Rudiløkken: It seems that the borrowing and lending market is in a positive trend and we think that this might be the picture in 2013 as well

The implementation of ESMA's new short selling regulations on 1 November introduced new standardised buy-ins across the region. Historically, buy-ins and punitive settlement penalties have been rare. A harsher settlement regime may be the catalyst for increased borrower demand as borrowers look to minimise exposure to increased fail costs.

Historically, many large institutional funds within the region have been very focused on corporate governance, and specifically, exercising their voting rights. We expect this theme to continue. Northern Trust has historically been able to provide creative solutions that allow beneficial owners to both lend and exercise these rights.

Burell: I am quite bearish in terms of returns. Equities are, according to most analysts, cheap now and that is probably true. Due to the macro economic / politic situation I don't anticipate a huge uptick on the risk appetite. Volumes and returns will stay low until you see some political stability in Europe.

Lewis: The market will be looking forward with optimism—the region is known for its innovation and technical advancement—and I would expect these skills to help participants in the region continue to develop their businesses into 2013 and beyond. **SLT**

Disproportionate engagement

Will Duff Gordon of Markit Securities Finance examines the immediate aftermath of the implementation of ESMA's short selling regulations

Regulators recently brought in public disclosure of pan-European short positions over 0.5 percent of a company. Now that the tide has gone out and we can see who is in the water, we ask ourselves how worried should corporate executives or investors be should their shares find themselves amongst those targeted by short sellers?

Being targeted by short sellers might be a daunting prospect for companies. Common perception will be that these investors stand to profit from any strategic slip that is made by management, essentially cheering on failure. While there is no denying that some investment strategies facilitated by short selling target underperforming companies, the research section of our website is replete with studies showing that short sellers add to market liquidity, prevent price bubbles and speed up price discoveries in markets.

Does it matter?

To gauge the implications of these disclosures, we dust off our academic gowns to survey the works and findings of Jones, Reed and Waller's paper Revealing Shorts: An Examination of Large Short Position. This report analyses the implications of share returns in the wake of large public short interest disclosure. We then ask ourselves what the applications of such news are to investors and companies that find their shares targeted in this week's round of disclosures.

Academic results

The research looked at European disclosure measures that were implemented in EMEA markets in the last few years. Without going into too much detail, Jones, Reed and Walker found that shares that were subject to short sale disclosures did not experience significant negative returns in the period following an announcement.

Waxes then wanes

The research did find that companies that were experiencing a rights issue did experience negative returns. However, this type of short selling falls in line with market arbitrage and hedging rather than outright speculation in share price movement. Also telling is the fact that while abnormal returns were negative immediately following the disclosure regime, this trend was watered down over time, ie, share prices drifted back up.

Tip of the iceberg and incomplete

Looking into the specifics of shares experiencing a short sale disclosure, the paper found that the disclosed short positions were only a small portion of aggregate short interest, indicating that public numbers were only the tip of the short selling iceberg. Moreover, short positions look to build immediately prior to a disclosure being made public.

Herding behaviour

Following a disclosure, the paper found examples of herding behaviour with shares experiencing a follow on disclosure being nearly three times more likely in firms that had a disclosure than ones that stayed out of short seller's cross hairs. This trend was most pronounced in firms that were targeted by large funds. Herding also seems to be geographically driven in that funds in New York or London were more likely to follow one another in disclosing positions. Far from discouraging short sellers, the disclosures actually stimulate follow on short selling immediately after a disclosure. This is both in publicly disclosed positions and undisclosed positions.

Public disclosure analysis

With these findings in mind, we turn to the wealth of disclosures following the European Securities and Markets Authority's (ESMA's) recent disclosure directive. On a like-for-like comparison versus what has been the case for the UK since 2009, the new pan-European disclosures differ with the disclosure threshold raised to 0.5 percent of a company's shares from 0.25 percent. Companies that are covered by the disclosure are widened from financials to the entire market.

From the first three days of disclosures, published by the UK FSA, we find 237 publicly disclosed short positions. These disclosures are spread out across 146 companies and have an aggregate value of $8.4 billion. The average aggregate short interest disclosed represents 2 percent of the targeted company's shares. Comparing the aggregate exposure disclosed with that in our system, we see that public disclosures represent roughly 53 percent of the value of short positions for the companies that were involved. When comparing the aggregate positions disclosed with the UK-wide short interest, we find that the proportion of disclosed short interest falls to 38 percent. This is obviously driven by large cap shares where a large amount of capital is needed to build a substantial short position.

Diving deeper into the public numbers, we find the usual suspects making up the majority of positions. It comes as no surprise that it takes significant capital to build up a 0.6 percent short position in Tesco, as is the case with Lansdowne Partners, which is the largest company to have a publicly disclosed position.

More to follow

Looking at the top 10 shares with the largest portion of their shares publicly shorted (more than 4.4 percent), the striking fact is that nine of these shares have an average of more than 10 percent of their shares short and undisclosed.

Perhaps more alarming is the fact that undisclosed short interest can be as high as 17.1 percent, as is the case in platinum miner Lonmin. We do see some shares with disclosed short interest greater than what is seen on our system, as is the case in BSkyB where public short interest is 2 percent higher than Markit short interest.

To conclude, we see from academic studies that publicising short positions does little in the way of moving share prices. Using our data, public short interest numbers fail to tell a consistent picture of what is going on in the market and that these disclosures tend to target small companies and large funds disproportionally. **SLT**

01 January

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17th Global Securities Financing Summit

Location: Luxembourg
Date: 16-17 January 2013
www.clearstream.com

The conference's 2013 theme is 'Expanding global reach: value creation through partnership'.

02 February

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19th Annual Beneficial Owners' International Securities Lending Conference

Location: New Orleans
Date: 28-30 January 2013
www.imn.org

IMN is pleased to announce that our 19th Annual Beneficial Owners' International Securities Lending Conference will be taking place January 28-30, 2013 at The Roosevelt New Orleans, LA.

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PASLA/RMA Conference on Asian Securities Lending

Location: Hong Kong
Date: 5-7 March 2013
ebiz.rmahq.org

This annual event combines the resources of both the Pan Asia Securities Lending Association (PASLA) located in Hong Kong and The Risk Management Association (RMA) located in the US.

04 April

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ISLA's 22nd Annual International Securities Lending Conference

Location: Prague
Date: 18-20 June 2013
www.isla.co.uk

Join your peers in participating in timely industry discussions on the latest legal and regulatory requirements, including a triparty repo reform discussion.

Industry appointments

J.P. Morgan has chosen **David Clarkson** to lead its prime brokerage operation in Europe, the Middle East and Africa (EMEA).

He joins the firm from Credit Suisse where he was most recently chief of staff in prime services. He will report to Teresa Heitsenrether, global head of prime brokerage, and will be based in London.

Clarkson helped to build Credit Suisse's prime services operation. He led its acquisition of Prime Fund Services from ABN Amro and held positions such as global head of prime security services and head of European and Asian prime services. He previously worked at Deutsche Bank as European head of equity swaps.

Heitsenrether said: "Since we launched our European prime brokerage offering last year, the amount of clients that we have welcomed onto the platform has outperformed even our own expectations. Clarkson's twenty years of experience and invaluable market knowledge will ensure that we continue to deliver on our promise, and stay closely aligned with our clients through product innovation and by drawing on the strength and breadth of our global offering."

Newedge has recruited **Aurelie Vincent** as a director for European capital introductions.

Vincent joins from Lyxor Asset Management in Paris where she worked in alternative investments on the managed account platform overseeing the CTA, global macro and fixed income desk.

She will continue to be based in Paris and will be responsible for growing Newedge's bespoke services in the CTA and global macro institutional investor segment, with a focus on France. She will report to Rebecca McVittie, the European head of capital introductions.

Duncan Crawford, co-global head of alternative investment solutions, said: "Newedge has been successfully serving hedge funds for over two decades. We have grown into the market leader and are best-known for our in-depth understanding of the sector and its specific needs. Vincent's experience and profound relationships are excellent additions to Newedge's unique service offering in the CTA and global macro space."

Omgeo has appointed **Jeff Kiley** as its new director of industry relations for the Americas.

Kiley joins Omgeo from J.P. Morgan where he held the role of vice president and managing director in prime services, based in New York.

In his new role, Kiley will focus on partnering with the industry to drive increased efficiency and reduced risk for the benefit of market participants.

Marianne Brown, president and CEO at Omgeo, said: "Kiley joins us at a time of momentous change across the financial services landscape. We look forward to having him join our team, and helping us to usher in the next wave of industry advancement."

Kiley said: "Omgeo plays such a critical role in the operational efficiency of the financial markets, and I'm honoured for the opportunity to participate. I look forward to contributing to key initiatives that will help Omgeo continue to decrease risk and enhance efficiencies for financial market participants globally."

It has been reported that Russian brokerage Broker Credit Services (BCS) has recruited high-frequency trading sales specialist, **Audrey Faveeuw**, from the London Stock Exchange (LSE).

Faveeuw worked as a development manager for the LSE, but according to reports, Faveeuw is joining BCS as a director for prime brokerage sales and will report to Tim Bevan, managing director and head of international prime sales.

Callan has recruited **Mark Kinoshita** as vice president to accommodate the demand for its trust, custody and securities lending services.

Kinoshita will be based in San Francisco and will report to Virgilio Abesamis, executive vice president of Callan's trust, custody and securities lending group.

Having worked in the securities industry for nearly 20 years, Kinoshita has experience in settlement operations, client reporting, client systems consulting, product and business development and project management.

Abesamis said: "I have known Kinoshita for many years and have always found him to be an honest, thoughtful, bold and collaborative person with the highest ethical standards; I am very happy to welcome him to the Callan custody team."

"Not only is the breadth of his knowledge and familiarity with every aspect of custody and back-office operations impressive, but he's truly committed to providing the highest-quality, personable service to clients." **SLT**

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