GLOBAL INVESTOR | ISF FOW

Securities Finance Americas Guide 2021

Summer 2021
www.globalinvestorgroup.com

SHORT AND SWEET

What does the move to T+1 mean for US securities finance?

TECH INNOVATION

TECHNOLOGY PROJECTS ARE LEADING THE CHARGE ON INNOVATION

PEER LENDING

THE GPFA IS BUILDING MOMENTUM IN THE US AND ABROAD

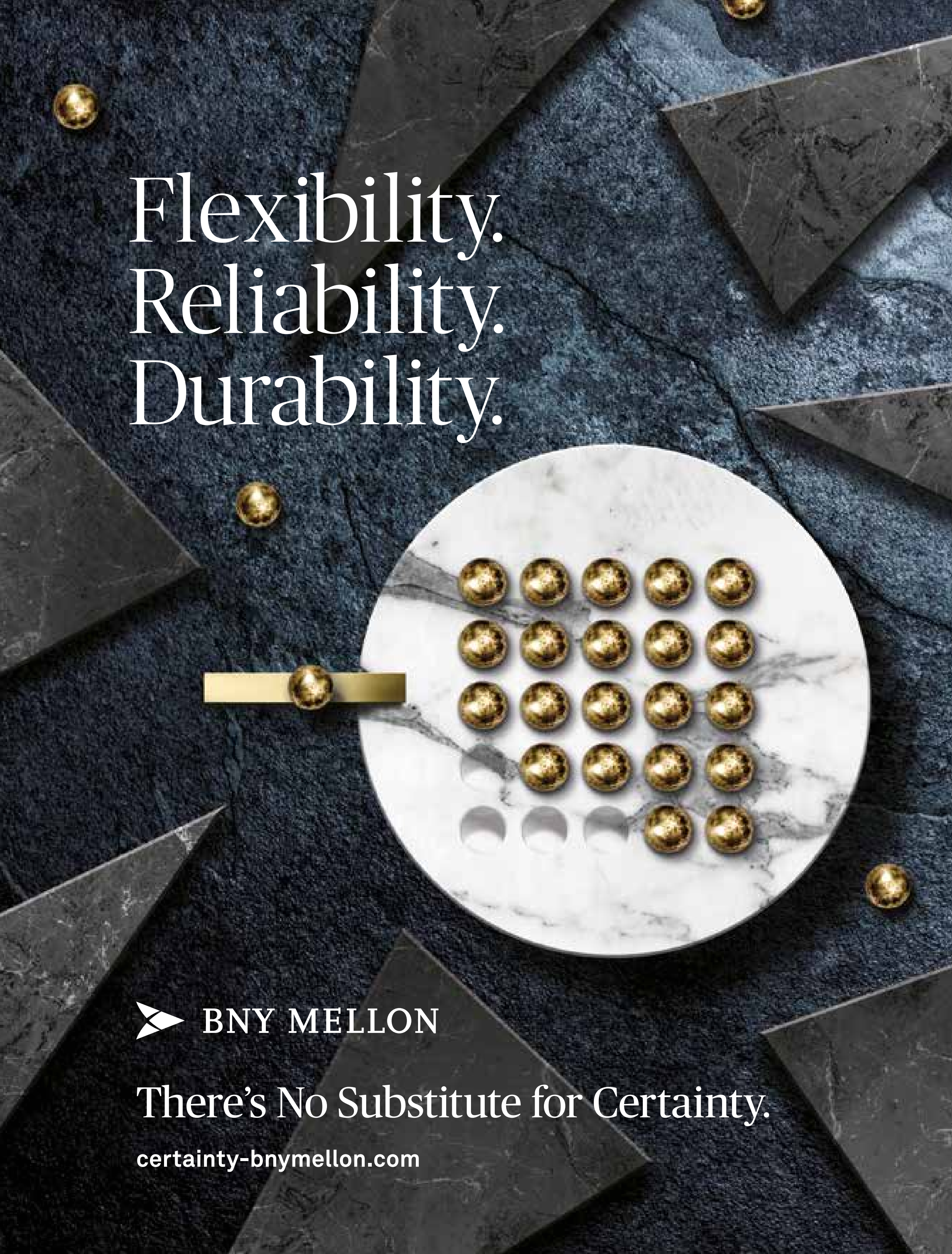
WOMEN IN SECURITIES FINANCE

The Co-Founders of the women's group talk about their latest developments

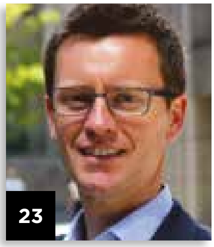
+ COUNTRY PROFILES

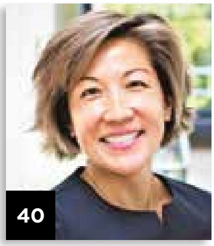
The latest securities finance developments in the region's key markets

Securities Finance Americas Guide 2021


Flexibility.
Reliability.
Durability.
BNY MELLON
There's No Substitute for Certainty.
certainty-bnymellon.com

Contents





GLOBAL INVESTOR GROUP | FOW | ISF

EDITORIAL

Managing editor
Luke Jeffs
Tel: +44 (0) 20 7779 8728
luke.jeffs@globalinvestorgroup.com

Securities finance editor
Oliver Wade
Tel: +44 (0) 207 779 8430
oliver.wade@globalinvestorgroup.com

Senior reporter
Perle Battistella
Tel: +44 (0) 207 779 8028
perle.battistella@globalinvestorgroup.com

Design and production
Antony Parselle
aparselledesign@me.com

BUSINESS DEVELOPMENT

Business development executive
Jamie McKay
Tel: +44 (0) 207 779 8248
Jamie.mckay@globalinvestorgroup.com

Divisional director Jeff Davis

Chairman Leslie Van de Walle

Chief executive Andrew Rashbass

Directors Jan Babiak, Colin Day, Imogen Joss, Wendy Pallot, Tim Pennington, Lorna Tilbian

© Euromoney Institutional Investor PLC London 2021

SUBSCRIPTIONS
UK hotline (UK/ROW)
Tel: +44 (0)20 7779 8999
US hotline (Americas)
Tel: +1 212 224 3570
hotline@globalinvestorgroup.com

RENEWALS
Tel: +44 (0)20 7779 8938
renewals@globalinvestorgroup.com

CUSTOMER SERVICES
Tel: +44 (0)20 7779 8610
customerservices@globalinvestorgroup.com

GLOBAL INVESTOR
8 Bouverie Street, London, EC4Y 8AX, UK
globalinvestorgroup.com

Global Investor (USPS No 001-182) is a full service business website and e-news facility with supplementary printed magazines, published by Euromoney Institutional Investor PLC.
ISSN 0951-3604

© Euromoney Institutional Investor PLC London 2021

Connecting supply and demand

Proponents of peer-to-peer securities lending are confident that rather than taking business from agent lenders, its wider use will facilitate deals that would not have happened in a conventional transaction environment.

Just over a year ago we reported on the launch of the Global Peer Financing Association (GPFA), which was formed to create a more efficient way of engaging in peer-to-peer securities financing transactions.

Board member Chris Benish, managing analyst at State of Wisconsin Investment Board (SWIB), says the industry has been supportive of the initiative since market participants realised that the association was not a trading platform or a substitute for an agent lender.

The GPFA has been careful to state that as it finds additional ways to connect supply and demand within the market, the whole market benefits and that peer-to-peer lending often represents incremental activity that simply wasn't happening previously.

"Not everyone will immediately sign a bilateral repo agreement with another pension fund, but maybe they will expand their approved counterparty list to include non-rated entities," he says. "Even among the founding members there are different approaches, different levels of engagement with peers and different routes to market."

The association view the expansion of peer-to-peer activity as risk-diversifying. Benish observes that SWIB's peer-to-peer activity allows it to expand the use of treasury/TIPS repo - which is at least 30-40 bps cheaper than equity financing - while for other entities it might mean expanding their securities lending programmes and boosting utilisation, which improves the profitability of the programme.

However, Benish acknowledges that institutional inertia can be a powerful force and that asset owners can be reluctant early adopters of a new route to market. "There are also a myriad of legal, operational and credit issues that need to be resolved," he adds.

Most of the agent lenders we contacted were reluctant to comment on levels of demand for peer-to-peer lending among securities finance clients, the potential benefits, and possible regulatory issues.

George Rennick, regional head of the America's agency securities lending at JP Morgan was more forthcoming, observing that indicators point towards increasing interest while accepting that it is difficult to quantify exactly how much demand exists.

"If the transaction was solely about economics, it would be reasonable to assume many lenders and borrowers would welcome the removal of intermediaries," he says. "However, those intermediaries have been proven to add significant value and support in the overall securities finance process. Examples of benefits provided by agent lenders include scale, efficiency, technology, global product expertise, oversight, operational support, trade life cycle management, counterparty strength, industry relationships, and indemnification."

Clients lending peer-to-peer could see an increase in economics on specific trades and increased utilisation for specific securities. It could also increase liquidity sources and reduce a lender's reliance on bank balance sheets, while for entities that operate group structures there may be opportunities to internalise liquidity flows.

"Lending directly requires an entity to staff and support securities financing to meet objectives, not on just a single transaction but on a portfolio of assets through the entire lifecycle," says Rennick. "One existing model in the peer-to-peer space leverages an agent lender to facilitate transactions and provide technology and product support as needed. For example, matching pension assets, an insurance fund or an asset manager portfolio directly with a prime brokerage hedge fund client could provide increased utilisation, especially for general collateral assets."

The obvious demographic for peer-to-peer lending are those global beneficial owners with an innovative approach to their securities lending programmes, such as the largest sovereign wealth funds and pension plans as well as sophisticated asset managers.

"These entities self-select because they are institutionally curious and are often amenable to new ideas, including the idea of dealing with new types of counterparts," observes Mark Faulkner, co-founder of Credit Benchmark, who

"Not everyone will immediately sign a bilateral repo agreement with another pension fund, but maybe they will expand their approved counterparty list to include non-rated entities."

– Chris Benish, managing analyst at State of Wisconsin Investment Board (SWIB)

says counterpart expansion or counterpart extension or even non-standard counterpart selection is perhaps a better way of characterising this activity since peer-to-peer implies activity only between a pension fund and a pension fund, for instance.

It could be argued that a hedge fund is not a peer of a pension fund, but the commonality is that they both use banks to interact, connect and intermediate - albeit for different reasons. A hedge fund would use a prime broker for more than pure market access, whereas non-levered funds could only use an agent for credit intermediation.

Participants in this market are looking to identify non-standard counterparts that they are confident in their ability to conduct business with, involving potentially a lower level of intermediation.

"There is also a requirement for both parties to have something the other wants," says Faulkner. "One example - albeit not a very common one - is where hot securities are sitting long in a pension plan that another plan wants to short in the market. This necessary 'coincidence of want' is much more likely to occur in collateralised lending or collateral upgrades."

A catalyst for this type of transaction might be that the traditional route to market via agent lenders is limited, blocked, or expensive.

The diversity of pension plans' requirements that occur due to demographic differences across countries and regions should also boost counterpart expansion as they will be investing in different products over different timeframes to address their different liability profiles. In addition, some of these plans will have cash requirements that can to be secured by equity or fixed income instruments or will want to be in the collateral upgrade business.

Faulkner says there is no reason why the peer-to-peer concept should not continue to gain traction globally, as long as participants understand the issues around market risk, the value of intermediaries, indemnification, and insurance.

"Digitised workflows will also make it accessible to a wider spread of pension plans, not just the largest and most sophisticated," he adds. "There is scope for technology to make peer-to-peer securities lending available to investment managers of all sizes, although the onus is on fund management groups to drive it towards their smaller fund customers."

He also believes there will always be a role for the agent lenders in areas such as settlement. "The peers will still need their bank or intermediaries for collateral management, the mark-to-market and other necessary operational services," says Faulkner. "The glamorous aspect of securities lending is doing the trades and finding new counterparts – the rest of the tasks involved could be done better but they remain vitally important."

In some cases, lenders will simply want to deal with higher rated counterparts – in this scenario the risk associated with peers lending to one another could be lower than if it were to be indemnified by a bank with lower credit quality.

Credit Benchmark's analysis of the credit ratings of the GPFA's beneficial owner, borrower and agent members reveals an average composite rating of AA-, A-, and A+ respectively. "Credit quality is a big issue – why would you pay for indemnification from someone with lower credit quality than a peer you could do business with directly?" asks Faulkner.

Chris Valentino, head of business development at Stonewain Systems, agrees that at this point the peer-to-peer approach is probably more suitable for those beneficial owners that are actively managing their securities lending programme, or at least a portion of that programme.

"There are a handful of beneficial owners in the market that are lending direct and those organisations have already done the legwork of setting up the internal infrastructure needed to support such a business," he says. "In addition to the technology and data needed there is also an element of subject matter expertise (trading, analytics, operations) required to support a direct lending programme."

Valentino says the cost of acting as a principal intermediary has been a driver of interest in peer-to-peer lending - with revenues under pressure, looking at all opportunities to further reduce costs makes a lot of sense. But he believes there needs to be a driver other than cost reduction.

"Additional sources of demand, stability of

“These entities self-select because they are institutionally curious and are often amenable to new ideas, including the idea of dealing with new types of counterparts.”

– Mark Faulkner, co-founder of Credit Benchmark

supply, improved pricing, diversification of counterparties, and increased distribution are all drivers of interest in peer-to-peer lending,” he adds. “Reasons why a fund might be reluctant to trade securities this way include knowledge and creditworthiness of the counterparty - there is certainly a level of comfort in lending to a large institutional broker dealer.”

It is important to note that peer-to-peer lending isn’t strictly defined. It could mean a totally different route to market with bilateral exposure between two non-bank/broker-dealer counterparts, but could also include just expanding approved counterparts within an agency model.

That is the view of Sam Pierson, director of securities finance at IHS Markit. “A common assumption is that peer-to-peer lending is driven by a desire to disintermediate traditional participants, but from what we observe the conversation is driving a deeper understanding of market intricacies and an appreciation of the value participants bring to their respective roles,” he says.

Peer-to-peer lending is therefore as much about engaging in different types of transactions and/or transactions that maybe cost prohibitive or have a different level of complexity. This supports Benish’s view that it becomes additive and increases the available means for lenders to distribute securities and increase earnings.

“Theoretically it should be applicable to all, especially if the approach is to just expand the approved counterparts within an agency model,” continues Pierson. “However, it requires the beneficial owner or asset manager to be more actively involved, whether that is in establishing, reviewing and approving new counterparts or actually executing transactions.”

For this reason, peer-to-peer lending won’t be suitable for all transactions, although it will be attractive for some lenders depending on

> **Even with the benefits of increased control and additional earnings, for some market participants this will not be a priority or they may not have the necessary expertise or bandwidth.**
>
> **– Sam Pierson, director of securities finance at IHS Markit**

operating model, asset mix and risk tolerance. The likelihood is that beneficial owners with internal expertise who are actively engaged in the securities finance markets are more likely to be in the first wave of adopters.

"Even with the benefits of increased control and additional earnings, for some market participants this will not be a priority or they may not have the necessary expertise or bandwidth," adds Pierson. "Peer-to-peer activity may also be conducted without an indemnification from an agent, which is an important factor for consideration."

On the question of whether the cost of acting as a principal intermediary has been a driver of interest, Pierson says it cannot be denied that the increased costs associated with additional capital and indemnification have negatively impacted loan balance growth.

"We have seen annual earnings stagnate around $9-$10 billion per annum over the past 10 years, while lendable securities have increased by 150% and now exceed $33 trillion," he adds. "While there are other reasons why there is increased interest in peer-to-peer lending, increasing capital costs is definitely one of the drivers."

As funds become more operationally efficient it could become easier for them to trade peer-to-peer suggests Bob Zekraus, COO and head of Americas at Pirum.

"If two parties or peers can get comfortable with the credit risk of transacting with each other, the need shifts to commercial elements, operational risks, and readiness," he says. "Operational aspects and requirements could be outsourced and managed on their behalf, with technology providers playing a big part."

The amount of information available through credit rating agencies means credit risk can be easier to quantify than operational risk, which could alter the conventional approach to securities lending.

"It would seem more natural for traditional beneficial owners, long holders and pension funds to be first adopters, but I believe hedge funds play a pivotal role as well," says Zekraus. "Benchmarking tools and products are available to assess the credit component, which could prove useful for the alternative community."

Of course, agent lenders might attempt to suppress demand for peer-to-peer lending by lowering the fees they charge borrowers and lenders and/or increasing efficiency in order to reduce their operating costs, but margins are already tight. The more likely scenario is that the banks accept their continued but perhaps slightly reduced importance, recognising that any trend that increases overall securities lending volumes benefits everyone in the industry. ■

Will peer-to-peer work internationally?

Having started out with four North American members with combined assets of less than $1 trillion, one of the key challenges facing the GPFA in particular and the peer-to-peering community in general was the extent to which the concept could gain traction in other parts of the world.

The GPFA has previously suggested that as many as 50 other pension plans wanted to be a part of the association. While still some way short of that total, membership now numbers 14 with total assets of close of $7 trillion and is starting to take on more of an international flavour.

Australian Super, Australia's largest superannuation and pension fund, became the first member from outside North America when it signed up in September 2020. More recently, two European beneficial owners - Norges Bank Investment Management and AXA Investment Managers – joined in December 2020 and March 2021 respectively. The latter's head of liquidity said joining the association would streamline the optimisation of excess liquidity and create an opportunity to partner on technology.

"There is demand for peer-to-peer securities lending in Europe and Asia and a number of European and Asian based beneficial owners/assets managers are either involved already or exploring this further," says Pierson. "It is already popular in Australia and we expect it to continue to gain momentum globally."

Valentino says his firm has not yet seen much demand for peer-to-peer securities lending from clients in these regions, but is quick to add that this does not necessarily mean that the demand is not there.

"One can certainly make the assumption that the global picture is being taken under advisement and it is possible that the market will take a regional approach to rolling out this type of trading, perhaps beta testing it in the US and then rolling it out to other regions over time," he says.

Regulation could have an impact on peer-to-peer lending in Europe. SFTR is a technology and operational- intensive set of regulations and it has taken quite some time for the traditional market participants to build the solutions that adhere to the principles of this type of regulation, adds Valentino.

"Would new entrants to peer-to peer have an appetite to build the appropriate infrastructure or would they look to outsource it? I think it comes down to whether or not the current intermediaries still play a support role in terms of infrastructure and operations."

Zekraus is another who is confident peer-to-peer lending could work outside of the Americas. "One would assume the nature of the transaction and outcomes are the same regardless of geography, but certain variables could be impediments - especially in more fragmented regions with potential regulatory hurdles and overall market adoption playing a critical role," he says.

At this stage it would seem that many organisations are sitting and waiting to see how the group expands and looks to change the way they trade, adds Darren Crowther, general manager of securities finance & collateral management at Broadridge. ■

Crossing borders

Michael Saunders, head of agency lending for the Americas at BNP Paribas Securities Services in New York, tells GI/ISF about its move to integrate cross-border flows into securities lending programmes, and the widening application of technology to all elements of the sector, including the fast-growing segment of ESG.

What internal changes are improving what your clients can expect?

In recent months we have seen several initiatives come to fruition, whose implementation began prior to the pandemic. These have strengthened our offering as an agency lender and, most crucially, enhanced the performance our clients can expect across all segments – from central banks and sovereign wealth funds through to leading asset managers, insurance companies and corporates.

The focus of several of these initiatives has been the integration of cross-border flows, leveraging our four different office locations in New York, London, Hong Kong and Sydney. This has improved the ability of local trading desks to employ all the assets held across a client's portfolio in securities lending transactions. In a low yield environment, the additional returns available to beneficial owners by maximising the use of their assets, wherever they are domiciled, is more important than ever.

"The focus of several of these initiatives has been the integration of cross-border flows, leveraging our four different office locations in New York, London, Hong Kong and Sydney."

What are the challenges of incorporating Asian assets into securities lending programmes?

The launch of our Hong Kong desk expanded our footprint in Asia. This is a continent where clients are seeing an increasing concentration of new investment opportunities and from where the effective mobilisation of assets for securities lending transactions has become increasingly valuable.

It is hard to overstate the importance of expertise in these new markets. Given the barriers to entry for clients, arising from the varied characteristics of execution and settlement across the region, they typically require a highly bespoke service. Our footprint in the region, established through our existing asset servicing businesses, means that we are familiar with precisely how the local regulatory and processing architecture is arranged.

This familiarity has been accumulated via a long history in the region: our lending desks

BNP PARIBAS

The bank
for a changing
world

In the UK, BNP Paribas Securities Services is authorised and regulated by the European Central Bank and the Autorité de Contrôle Prudentiel et de Résolution. Deemed authorised by the Prudential Regulation Authority and with deemed variation of permission. Subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details of the Temporary Permissions Regime, which allows EEA-based firms to operate in the UK for a limited period while seeking full authorisation, are available on the Financial Conduct Authority's website. BNP Paribas Securities Services London Branch is registered in the UK under number FC023666. UK establishment number: BR006393. UK establishment office address: 10 Harewood Avenue, London NW1 6AA.

> **“We are approaching a point where we are genuinely agnostic when it comes to where the client is based. Our mind-set has shifted to the domicile of the asset rather than the location of the client.”**

are just the latest addition to a servicing infrastructure that stretches back many years. This history began with our custody network, through which we have developed a granular understanding of the local regulations and often highly bespoke settlement processes. In turn this understanding has allowed us to support credit opportunities and expand the range of products developed by our teams on the ground. In other words, the BNP Paribas flag had long been planted: the recent establishment of our securities lending desk has allowed clients to harness this existing network, monetising assets in their securities lending programmes that historically they had been unable to use.

The benefits become clear when you consider the case of a US client owning Hong Kong or Australian assets. Given the time difference and the lack of a local presence, the practice of placing those assets on loan previously was very rare. It involved going through European or US brokers, with the opportunity set limited to intrinsic-based lending. Clients therefore often missed out on high fee opportunities presented by assets they owned that were in particularly short supply.

Today, for clients domiciled in regions beyond Asia, utilisation of Asian assets has increased. And this isn’t just around specials. Unlike other providers, whose balance sheets may restrict them in supporting lower-margin collateral transactions, we can support general collateral trades. We are approaching a point where we are genuinely agnostic when it comes to where the client is based. Our mind-set has shifted to the domicile of the asset rather than the location of the client.

Why is seeking out additional liquidity important to clients now and how are you helping them achieve it?

Working to better identify hidden pockets of liquidity for our clients is a second area where we have recently been focusing our efforts and one which closely supplements this more global lending model previously discussed.

With such an excess of liquidity in the market, clients continue to find it very difficult to discover short-term investments or collateral types that offer a competitive yield. The current records being set in the use of the US Federal Reserve reverse repo programme, where daily deposit balances were more than $750bn in late June, despite the programme offering a zero-interest rate, demonstrate this conundrum. (Please note record usage exceeding $765 billion daily following the recent FOMC action to raise the RRP floor to 0.05%)

It falls to agent lenders to do everything within their power to search out additional revenue opportunities. This includes forging partnerships with leading technology vendor’s and we have recently struck an arrangement with execution vendor HQLAx, an investment that dramatically improves our ability to identify liquidity opportunities of this type. It is one of many partnerships we have with vendors that improve our ability to tact pockets of liquidity.

What is the contribution of collateral transformation to these efforts?

This is another area in which we have invested heavily in recent years, in response to the growing demand for HQLA. Providing the means by which clients can lend such assets against other high-quality liquid assets means releasing an important source of

> **"DARLS means that we can invest cash on behalf of the client in the market via a list of approved counterparties while providing an indemnification against counterparty default."**

additional return without exposing clients to a deterioration in creditworthiness.

Consider the case of lending out US Treasury bills in exchange for UK gilts and earning a spread from the trade. This may only generate seven or eight basis points of spread but at the scale of $1bn or $20bn the revenues that accrue can be considerable. In addition, this is a stable and predictable revenue stream, making it a valuable additional strategy that can be incorporated into a securities lending program. We've seen great traction here recently with a range of clients from central banks and sovereign institutions to large asset managers.

Another particularly popular shift recently has been the growing practice of assisting clients with the investment of their short term excess cash outside of their lending programme. Utilizing our existing infrastructure and expertise to find pockets of opportunity in the short term interest rate space in accordance with defined risk parameters has proven to be impactful in fortifying existing client relationships. Once again, this is being driven by the low-yield environment. Across the board, beneficial owners such as corporates, pension funds and sovereign wealth funds are all long cash and are looking for ways to use it. Our offering provides a solution to this problem, giving a short-term management tool able to generate enhanced yield over traditional money market products including money market funds, Treasury bills or term deposits.

How are you helping clients find ways to reinvest cash collateral?

Much of what we've discussed so far has focussed on lending an asset and receiving the cash or non-cash collateral in return. An important second leg to this process is reinvesting collateral when it comes in the form of cash. That is where our new product Directed Agent Repo Liquidity Solution (DARLS) is relevant. . It allows us to leverage our strengths in infrastructure, documentation and risk monitoring, and our operational support network.

DARLS means that we can invest cash on behalf of the client in the market via a list of approved counterparties while providing an indemnification against counterparty default. This combination ensures the investment is secure and highly customised in terms of tenure and approved collateral. It works almost like an ancillary business leveraging off the agency lending desk, offered to clients of the bank within their existing program and focussing on the excess cash they are looking to deploy. In effect, it means clients can outsource liquidity management on a daily, weekly, monthly or quarterly basis and we have already seen the product gain a high degree of traction among our clients.

How important is ESG becoming and what specific challenges does it impose when it comes to securities lending?

The issue of ESG could hardly be more topical. It is an agenda item on every client review, and every proposal we read contains a section devoted to it. Across the investment industry, the question of whether an ESG strategy is producing a tangible impact in the world is under considerable scrutiny.

When it comes to this growing demand for transparency, securities lending is no exception. In our sector, the focus lay initially

> **At our core, BNP Paribas' ambition is to participate in building a more sustainable future. As a leader in the ESG space, we believe we have an important role to play which is highlighted by our global initiatives.**

on issues such as recalling securities for proxy measures – such as AGMs and other votes – and most agent lenders today are able to accommodate requests of this kind.

But industry efforts are now expanding into areas such as how quickly and easily ESG-approved collateral sets can be processed. . We are heavily involved in these efforts both within our organisation and at industry bodies to not only monitor the ongoing development but assist in the shaping of pertinent parameters to apply ESG criteria to a securities lending programme. Our involvement with the industry working trade groups combined with the focus of BNP Paribas to become the leader in ESG enables us to be well versed in the issues that matter to both the agent lender and the beneficial owner communities. At our core, BNP Paribas' ambition is to participate in building a more sustainable future. As a leader in the ESG space, we believe we have an important role to play which is highlighted by our global initiatives. These ambitions are core principals of all our businesses and we strive to incorporate this into the management of our securities lending programme.

To achieve ESG compliance in securities lending programmes requires a robust infrastructure on the part of the agent lender, supporting buffered access and imposing restrictions on incoming collateral. Here, our position as a leading custodian puts us at an advantage since that infrastructure is securely in place. We are accustomed to providing highly bespoke and customised solutions when it comes to shifts in client demands, such as the recent trend for placing restrictions on specific asset classes or names. Here again we are in discussion with several external technology vendors in this space further to improve our offering.

How far can technology play a role in scaling these new offerings?

In part due to many of the trends that we have discussed here, we anticipate significant growth to our agent lending business in the coming months and years. A high level of automation is required to facilitate that growth whilst maintaining the highest quality of service. It is no secret that increasing automation in the securities lending process to remove time consuming manual elements is an important priority for providers and clients alike across the sector. We are pursuing our strategy to achieve both, by developing solutions internally and by expanding our partnerships with external providers.

In the second case we are in discussions with a number of external firms who are pioneering the latest applications of technology, such as AI. The application of technology has made big inroads already in sparing teams the monotony of manual processing across almost every element of the trade lifecycle, including processing recalls and their return elements and all components of corporate actions. But there is a lot agent lenders can still do to make the securities lending processes more streamlined, more efficient and faster. Harnessing the cutting-edge solutions provided by external specialists is an essential way to harvest the additional benefits on offer. Like all agent lenders we are working hard to make this element more streamlined and seamless. ■

Adapting to change in the US equity market

Market experts discuss how a shortened US equity settlement cycle will impact the market and identify key areas that must be addressed.

The Depository Trust & Clearing Corporation (DTCC) in February called for the world's largest equities market to move to next-day settlement (T+1) by 2023, the US having been on a T+2 settlement cycle since 2017.

The call for shortened settlement came after a period of heightened volatility in the US market, largely caused by a series of orchestrated moves from retail investors actively taking a stand against Wall Street in January. Individuals that met through social media platforms, such as Twitter and Reddit, and one SubReddit in particular, WallStreetBets, piled into certain stocks in response to activist short sellers disclosing their short positions in specific companies. The most famous "meme stock", as they became commonly referred to, was gaming retailer GameStop, that witnessed its share price soar in January to highs of around $500, causing short sellers to lose more than $5 billion in the month.

Michele Hillery, general manager of equity clearing and the DTC settlement service at the DTCC, insists that the call to shorten the US settlement cycle was not in response to these events. She says: "Our conversations with the industry around the move to shorten settlement cycles have been ongoing since early 2020, and well before 2021 events. However, there is no doubt that the recent increased focused on an accelerated settlement cycle has been partly driven by recent volumes and volatility in US equities markets."

"Accelerating the settlement cycle will have many benefits such as reducing systemic risk, operational risk, liquidity needs, buy-side counterparty exposure, and broker-to-broker counterparty risk."

– Michele Hillery, general manager, equity clearing and DTC settlement service at the DTCC

George Rennick, head of agency lending in the Americas and global head of client relationship management in agency lending at JP Morgan, believes that January's affair, and the continued volatility surrounding certain stocks thanks to retail investors, may be a catalyst to push the agenda forward. He notes that the industry is "taking a hard look" at the existing trade flow and is in the process of determining if there is a need for enhanced control and revisit of the T+1 cycle.

The DTCC has been advocating for a move to shorten settlement cycles for "well over a year", Hillery claims, noting that a shorter cycle brings enhanced market resilience, reduced margin requirements and lower costs for investors. She adds: "Accelerating the settlement cycle will have many benefits such as reducing systemic risk, operational risk, liquidity needs, buy-side counterparty exposure, and broker-to-broker counterparty risk. For broker dealers, a move to T+1 should lead to a reduction in margin and collateral requirements.

"For investors, a move to T+1 will allow their transactions to complete more quickly, while providing faster access to their funds following trade execution and settlement. Another benefit of shortening the settlement cycles – for all market participants - will be the further mitigation of systemic risk by reducing the exposure between the counterparties to a trade, between the counterparties to the clearing house, and for the clearing house itself."

Murray Pozmanter, head of clearing agency services and global business operations at the DTCC, estimates that switching to T+1 would remove 41% of the volatility component of the margin requirement, which makes up around 60% of the total margin requirements. He calculated that the move would save the market around $250 million per day and, during periods of extreme volatility, upwards of $7 billion per day.

The market infrastructure organisation led the industry-wide initiative to shorten the US equity settlement cycle from T+3 to T+2, a move that Hillery describes as "the most significant change" to the securities settlement cycle in more than 20 years. She continues: "Based on in-depth industry feedback which DTCC has received over the past six to nine months, we believe that now, more than ever, there is consensus amongst market participants to move to T+1. In order to help facilitate this move, we are collaborating with the Securities Industry and Financial Markets Association (SIFMA) and the Investment Company Institute (ICI)."

But Rennick is unsure now is the right time to try and shift the market to a shorter settlement cycle given the current market conditions, despite agreeing that the move is in the best interests of the market. He explains: "It's difficult to say that the proposal has come at the right time, particularly given that we're in a global pandemic where everyone is trying to adjust to a new way of working, while also managing a return to the office strategy. But, given the significant spike in trade volumes and corresponding exposures paired with the benefits of advancement in technology and automation, a move to T+1 seems like a prudent

"The existing two-day period to settle trades exposes investors and the industry to unnecessary risk. There is no reason why the greatest financial system in the world cannot settle trades in real time."

– Robinhood co-founder and chief exec Vlad Tenev

and correct move. However, trying to pull that off in the next 24 months does not seem like the best use of immediate focus and resources."

Online trading venue Robinhood was heavily scrutinised earlier in the year for halting the buying of GameStop shares on its platform in response to the heightened volatility. The affair caused the trading platform to default on its margin call from the National Securities Clearing Corporation, the central counterparty subsidiary of DTCC, after it made a call of $3 billion, which Robinhood co-founder and chief exec Vlad Tenev said was an order of greater magnitude than the firm had previously experienced.

Shortly after the incident, Tenev insisted the current T+2 cycle exposes the industry to "unnecessary risk". He said: "The existing two-day period to settle trades exposes investors and the industry to unnecessary risk. There is no reason why the greatest financial system in the world cannot settle trades in real time. I believe we can and should act now to deploy our intellectual capital and engineering resources to move to real-time settlement. Together we can solve this."

The move to a T+1 settlement cycle has not yet been approved by the US Securities and Exchange Commission (SEC), but DTCC has engaged with the regulators and they will be discussing specific rules changes that may be needed in the coming months, notes Hillery.

Rennick believes that the move to T+1 will likely result in a reduction of operational and system risk, meaning that the regulatory bodies would "support any move" that contributes to the removal of inherent systemic risk. Gary Gensler, who was appointed chair of the SEC in April, has been vocal about his interest in a shortened settlement cycle, which suggests that regulators could approve the move.

The JP Morgan executive suggests it is not technology preventing the move to T+1 from happening at a faster pace. He says: "It's worth highlighting that the technology at the DTCC already exists to settle US Equities on a T+1 cycle and a number of market participants already take advantage of it on an as-needed basis, but it has not been adopted more broadly. Every major institution globally has participated in the reduction of trade settlement cycles, multiple times, and so it certainly can be done."

"Given the significant spike in trade volumes and corresponding exposures paired with the benefits of advancement in technology and automation, a move to T+1 seems like a prudent and correct move."

– George Rennick, head of agency lending in the Americas and global head of client relationship management in agency lending at JP Morgan

Given that the technology needed for an even shorter settlement cycle than T+1 is readily available and has been used my market participants in the past, some may ask why a move to T+0 is not preferable. When you factor in the reduced operational and systemic risk that a shorter cycle brings, alongside the cost saving benefits, many would argue that reducing the settlement cycle as much as possible is the correct move, particularly when this cycle, and technology, is being used already.

However, DTCC's Hillery believes that moving to a T+0 settlement cycle is "not feasible at this time". She argues: "While DTCC supports T+0 settlement today - processing over 1 million same-day transactions each day with most settling instantly and using existing clearing and settlement technology - an industry-wide move to T+0 is not feasible at this time. This is because currently, not all industry participants are capable of moving to a T+0 settlement cycle, partly due to legacy business and operational processes which would not be able to support current trading volumes or existing business structures and may introduce additional risk into the system."

Transitioning to a T+1 settlement cycle allows the industry to retain the risk-mitigating benefits of netting, which frees up billions of dollars in margin that would otherwise be moving through the market at any time. The additional day also provides brokers with sufficient time to arrange for the financing that allows investors to buy securities on margin, which is a loan from the broker to the investor. Trying to carry out these tasks on a T+0 settlement cycle would be significantly more challenging, notes Hillery.

Rennick underlines the importance of retaining efficiency when moving to a shorter settlement cycle, as he highlights that some of the benefits also bring new challenges. He continues: "When I think about the US equity market moving to T+1, one of the biggest challenges in my mind will be to maintain efficiency in settlements and funding, because US equities already settle in a very efficient manner."

Shortening the cycle involves complex processes and shortening it will require extensive due diligence to identify operational and business impacts. To minimise the impacts, the DTCC is in the process of trying to identify and analyse the key products, markets, and processes that will need to be modified to accommodate the move to T+1. Areas identified so far include securities lending, foreign exchange, the impact on institutional trade processing, financing and segregation requirements, as well as processes such as post-trade affirmation and broker processing.

The greatest impact of a shortened settlement cycle on the securities lending market would be a "significant increase" in recalls and recall fails, which in turn could lead to increased outright trade settlement fails and buy-ins, explains Rennick. In the current T+2 cycle, investors benefit from having an additional day to make decisions and satisfy needs. For example, it affords them the opportunity to make security substitutions and issue recalls to borrowers for example.

The DTCC is working with SIFMA, which represents the US securities industry, and the ICI to agree on the key steps to shortening the cycle for secondary market transactions and identify priority issues. The two bodies have previously expressed their support of shortening the US equity market's settlement cycle. The DTCC hopes to complete its analysis on the next steps to achieving T+1 by the end of September and will shortly after develop a definitive timeframe for moving to the shortened cycle.

Rennick stresses that all corresponding regulations that are attached to or dependent on settlements must be adapted to fit the new cycle and must be ready for the time T+1 goes live, underlining that the settlement standard cannot be changed "in isolation". ■

DLT: the new frontier for securities lending

The OCC is preparing what is likely to be one of the world's largest enterprise-wide applications of distributed ledger technology. Testing of OCC's new securities lending transactions platform could begin as early as next year. In conversation with **Matthew Wolfe,** Executive Director for securities finance at OCC, GI/ ISF got a look at how the new system will work and what advantages it will offer users.

Can you explain a little about your current system and how distributed ledger technology will change it?

Currently there are two programmes that OCC offers: the Hedge Programme created back in the 1990s which has approximately $132bn in balances (as of 6/21/21), and the Market Loan Programme created in the late 2000s and now operated by EquiLend Clearing Services. OCC's new distributed ledger technology (DLT) platform will support both of those programs in the way that the current system does. In addition, the new system and OCC's rules will support a new hybrid programme that will be the foundation for future product and service enhancements.

Currently, in the case of Hedge, once the lender and borrower have negotiated the loan, the details are sent to DTC. Following the delivery versus payment confirmation OCC records and guarantees a loan between the lender and the borrower.

The delivery confirmation of the current system does not include the terms of the loan (e.g. the dividend rate, the rebate rate, any term structure, etc.). This creates gaps in what OCC can guarantee, limiting the extent to which OCC can provide a more complete novation for counterparties on all aspects of the contract, and causing the lender and borrower to have some residual bilateral credit exposure.

The new system will accept bilaterally negotiated loans from a range of participants. Transactions that are arranged on a trading platform can be submitted by the platform on the parties' behalf. Alternatively, parties themselves can submit directly and OCC will confirm that the terms of the loans sent by each party to the transaction match before sending instructions on to DTC for settlement. By confirming that details from the lender and the borrower align, errors will be identified before, rather than after the fact. It also means that OCC has full contract details allowing for more complete novation. This also means that the new system must handle a wider variety of life-cycle events including changes to rebate rates, recalls, buy-ins, etc.

Why did you choose distributed ledger technology to underpin the new system?

DLT allows users to track a securities lending transaction through all its steps through the entire life-cycle via a single immutable

> **DLT allows users to track a securities lending transaction through all its steps through the entire life-cycle via a single immutable ledger. This includes the initial submission and settlement, daily marks, post trade activity, and eventually the contract's termination.**

ledger. This includes the initial submission and settlement, daily marks, post trade activity, and eventually the contract's termination. DLT is particularly well suited to stock loans because these are bilateral contracts that must be managed correctly. Transaction activity as well as the state of the contracts – current and historical – can be seen by parties that have adopted a node which allows them to monitor the shared ledger (presuming they are entitled to see the activity and positions).

Users can stay connected to OCC and any relevant counterparties, confident that they are working off exactly the same version of the contract as the counterparty. Rather than waiting for a daily update, the state of a contract is visible in real time. The clarity of the record and the speed of communication are some of the DLT's biggest strengths.

OCC is taking a gradual and pragmatic approach to DLT though, settlement still occurs off-chain at DTC; cash will still be handled through bank accounts: nothing is tokenised in this process, although we are well positioned if the market goes in that direction – it's about sharing information more effectively.

For those unfamiliar with distributed ledger technology, can you provide an explanation of the benefits?

One way to think about this is the shift from CDs to streaming music. CD technology required significant infrastructure from both the distributor and the consumer of the music. The producer would burn a copy from a master track onto a CD, package the disc and ship it off to fans. Those fans would need a CD player, a receiver, and speakers to play music. When a fan received or purchased the CD, they would first have to unwrap the CD (remember that horribly difficult plastic theft resistant packaging), place it in the tray, and then press play in order to hear the music. Both producers and receivers needed to take several actions in order to publish or listen to the music. Streaming services dispensed of the need for much of this infrastructure and made the publication and enjoyment of music much more efficient. Now, the producer stores the master copy in a format that is immediately available to anyone with a streaming device, be that a mobile phone, a virtual assistant or a computer. For the user, the initial investment is lower and playing music can be as easy as saying, "Play my favourite band".

Currently OCC's role in the securities lending industry is much like the distributor of music CDs. OCC creates files of information about transactions and contracts on a daily basis. Those files then have to be distributed through a variety of means to clients, each of whom need specialized systems to decrypt and unpack the file, extract the information, load it in to their own systems and then compare it to their own internal books and records. The ledger provides an always available and definitive record of this information that is available to anyone with permission to access it. Decrypting, unpacking, and parsing is all taken care of by the node, just like a smart speaker. Clients no longer need to buy and maintain the legacy infrastructure, and what you do with the information is up to you.

Nodes can be located in a data centre or in the cloud, and they allow users to customise the format, type and frequency of updates

OCC Stock Loan Programs

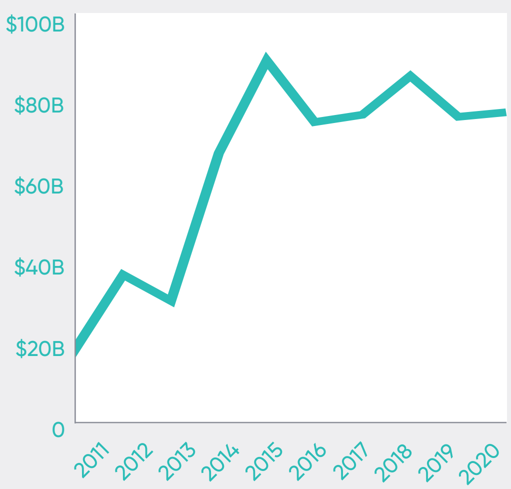
Key Benefits

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

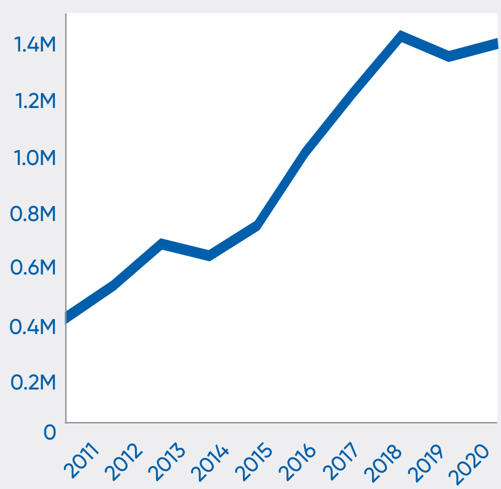
79
HEDGE LOAN PROGRAM MEMBERS

101B
AVERAGE DAILY LOAN VALUE AT YEAR END 2020

Annual Notional Value of Loans



Annual New Loan Transactions



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

Copyright © 2021. The Options Clearing Corporation. All rights reserved.

they receive. Some users may use a node to continuously synchronize with a traditional database, from which information can be queried or extracted in familiar ways. Other users can choose to adopt a node that provides updates each time there is an update to one of their transactions or contracts. These updates can be published via standard messaging protocols.

The system is also backwards compatible; OCC will still support screens, and we will still have XML messages. Users can stay on their existing systems for as long as they want, and clients can choose if or when they want to explore adopting a node and testing its functionality. There is no need to co-ordinate their adoption with that of their counterparties. Of course, the benefits can be greater if both sides employ a node, as they will have a constant view of the immutable version of their contracts and activity.

Why is OCC able to harness the DLT in this way before other parts of the sector?

OCC is uniquely positioned to harness the benefits of DLT on behalf of its participants. We are a trusted entity at the centre of the securities lending market, which means we aren't reliant on the widespread adoption of a new technology to make it work. This privileged position allows OCC to offer up the innovations and efficiencies of a technology like DLT and let users choose how and when to engage. In so doing we are delivering on OCC's broader objective to support a sound and secure foundation for the markets we serve, while at the same time helping the industry innovate, grow and become more efficient.

"We are a trusted entity at the centre of the securities lending market, which means we aren't reliant on the widespread adoption of a new technology to make it work."

It's important to see all this in the context of the wider progress that technology can deliver for the industry. OCC's focus has always been on using technology to address industry pain points while generating ideas that will help propel the industry forward in the long run. Facilitating this growth is our focus. We want to help make reconciliation easier, increase the accuracy and timeliness of members' books and records, and reduce the associated risk of inaccurate, delayed, or incomplete information. By using DLT we can achieve significant progress towards these goals at a price point that compares to our current systems. OCC embraces this opportunity to help the industry grow in this way, while at the same time not forcing it in any particular direction.

When can users start to use the new platform?

OCC worked to develop a proof of concept in 2019. Since then, we have demonstrated the system to a wide variety of OCC clearing and non-clearing members. We followed up on those demos with interviews that generated a collated set of user feedback. We were pleased to find the reception was much more positive than we had expected. The majority of users said that they were very supportive of the new system and highly likely to adopt it. Some said they would adopt the technology immediately; others said they were likely to start using the information provided by the ledger to compare with their existing records.

OCC is close to a point where we can demo the system and potentially begin testing as early as 2022. We will work closely with members to educate them on the various functionalities and what it means in practice to adopt a note. Information will be published via the Renaissance section of our website, www.theocc.com. ■

End to a long wait

GI/ ISF looks at three current applications of the ledger and machine learning that move cutting edge technology beyond proof of concept and into bottom-line savings.

In February, announcing a partnership with Google Cloud in US Treasuries, BNY Mellon claimed its new tool could forecast four out of ten settlement fails before they occurred. The firm's executives pointed to the roughly one in 50 US Treasury transactions resulting in fails: clearly, the cost savings associated with an effective solution like this could be huge.

It was a typical announcement. Barely a week goes by without a new launch that promises millions of dollars of savings from the latest AI or blockchain technology.

The technology – which in BNY's case harness Google's cloud-based machine learning resources, to predict likely fails on the basis of the features of past cases – is intuitively appealing. And for hard-pressed securities lending participants, large payoffs seem close within reach (For example, why couldn't an AI sifting through enough historical data predict future demand and let owners of securities focus their efforts on where they will find the best lending rates). And framed in the terms of the BNY announcement, for the clients of agent lenders or tri-party providers, the business case seems compelling.

Indeed, a few cases where individual vendors and major infrastructure participants are making headway alone have emerged. Global Investor/ ISF looks at examples swapping talk of proof-of-concept to impact onto the bottom line.

1. Matching and machine learning: SmartStream

Applying machine learning to improve matching accuracy can create cost savings of up to 20%, says Nathan Gee, marketing director at SmartStream, which launched its Affinity AI product in October. "If your reconciliations take in millions of transactions per day, [the savings] can be considerable."

Machine learning allows the automation of once-manual tasks while retaining the dynamic nature of manual intervention. It acts as a virtual user: the more it observes, the more efficient it becomes.

Matching presents a particularly rich set of opportunities. For example, where low quality data fails to identify a broker, an AI can spot this from previous manual matching instances with similar data platforms. "Straight away, your match states can increase and your reporting improves, and you can find which brokers are not providing you with sufficient detail," says Robin Hasson, product manager for TLM Reconciliations at SmartStream.

Smartstream's machine learning plugs into the company's existing reconciliation products, boosting matching rates and removing disruptions and delays created by anomalies, which are now spotted before they get too far downstream.

It also automates static data look-ups that have been managed manually, learning via historical data from manual matching. Where poor information in fields like trade reference, asset identifiers or currency codes are not covered by the static rules, data is predicted by AI and made available to the matching engine.

Transparency around how the AI plugs such gaps helps secure buy-in from client teams, says Hasson. "The system gives a confidence score for the prediction and how and why it reached that conclusion."

Typically, SmartStream conducts a review with a client to identify where the technology offers most bang for its buck. "There's no point using it where you're getting a 99% match rate on payments," he says. Installation involves setting up a few APIs to run on scheduled basis and configuring these with the existing standard processing flow with the technology hosted on the client server or the cloud.

The solution has been evaluated by three clients, one of which is employing it. Adopted at scale, it could yet have a large impact: SmartStream's reconciliation solutions are employed by 70 of the world's 100 largest sell side firms.

2. Machine learning in order management: FIS Global

Elsewhere, machine learning is helping dealers identify the most promising enquiries from hedge fund clients, allowing them to focus their energies on opportunities most likely to lead to business.

Hedge funds bombard their broker dealers with thousands of enquiries every hour with only a tiny fraction likely to lead to orders. AIs can spot the patterns in historical enquiries, adjusting as they change, pulling out the most

"Straight away, your match states can increase and your reporting improves, and you can find which brokers are not providing you with sufficient detail."

– Robin Hasson, product manager for TLM Reconciliations at SmartStream

promising leads based on those that resulted in orders historically.

"These are the ones you want to put to your agent lenders; the rest is noise," says David Lewis, of FIS Global in London, which has been running an AI hedge fund order manager for "a handful" of brokers dealers for roughly a year.

Machine learning also gets round an unintended consequence of automation where the absence of human oversight removes the chance to adjust processing standing settlement instructions (SSI).

Removing people from the process increases efficiency, reduces costs and improves accuracy. But with no eyes on a task, there is no one to gather insights from the data it throws out. Among prime brokers and agent lenders, where the majority of operations are automated, machine learning can provide this missing oversight, learning much quicker than a human would.

Say an agent lender is considering which funds to source portions of a borrow order from. Fund B 'churns' its portfolio more than fund A, turning over positions with greater frequency, something the AI has learned from previous instances where the agent lender used that fund's stock.

On the face of it, fund A would be a better choice: the trade is more likely to continue to duration, avoiding the costs associated with a recall, which include shifting the collateral and reporting the new details under ESMA's SFTR rules. But there are other costs to consider beside those associated with a recall. Consider those arising from delivering the collateral required by that fund or those from the marginal change in exposures to the fund's counterparty. These need to be calculated, weighted and fed into the decision to identify the most economic match.

So far, so algorithmic. There's nothing here that you couldn't build using standing settlement instructions (SSIs). But that would

Machine learning also gets round an unintended consequence of automation where the absence of human oversight removes the chance to adjust processing standing settlement instructions (SSI).

be static. The rules would be based on a set of historical information that would become progressively more out of date. When the world moves on – a fund tweaked its strategy, moving to a longer-term holding strategy for US equities, for example – SSIs get left behind. By contrast, AIs never stop learning.

Lewis sees a time not far in the future where funds occupy different 'smart buckets' - discrete categories, to each of which is attached a price at which it is economic for the agent lender and borrower to trade. Funds may occupy different buckets depending on the asset – as where a fund has a high churn rate for US equities but a low rate for UK Treasuries. They may do so depending on the structure – since a loan, repo or total return swap may carry a different break even for the same fund. Or they may do so for different collateral types – a fee that is attractive for a straight stock trade with a fund may be uneconomical for one using pledge, cash or non-cash collateral.

3. Efficiency gains from Distributed ledger technology (DLT): HQLAx

Elsewhere, DTL is being used to take a bite out of up to €3.65bn in unnecessary compliance costs banks are paying to manage Liquidity Coverage Ratios (LCR).

According to a recent report from Basel Committee on Banking Supervision, the average Liquidity Coverage Ratio of Group 1 banks is 138%. This corresponds to €13.4trn of HQLA, or €3.65trn more than they need to hold according to the 100% LCR required by regulations. Oliver Wyman estimates the opportunity cost of holding €3.65trn back for the LCR that could more profitably be used elsewhere is roughly €3.65bn.

The main reason the buffer is so much larger than it could be, is because collateral management is slow and clunky. Specifically, banks must build in capacity for the delays from slow operational processes and settlement fails.

HQLAx, a securities lending platform that has been live since the end of 2019, harnesses the blockchain to eliminate many of these inefficiencies. It does so by allowing two parties to transfer the ownership of securities between them without an equivalent transfer between their chosen custodians.

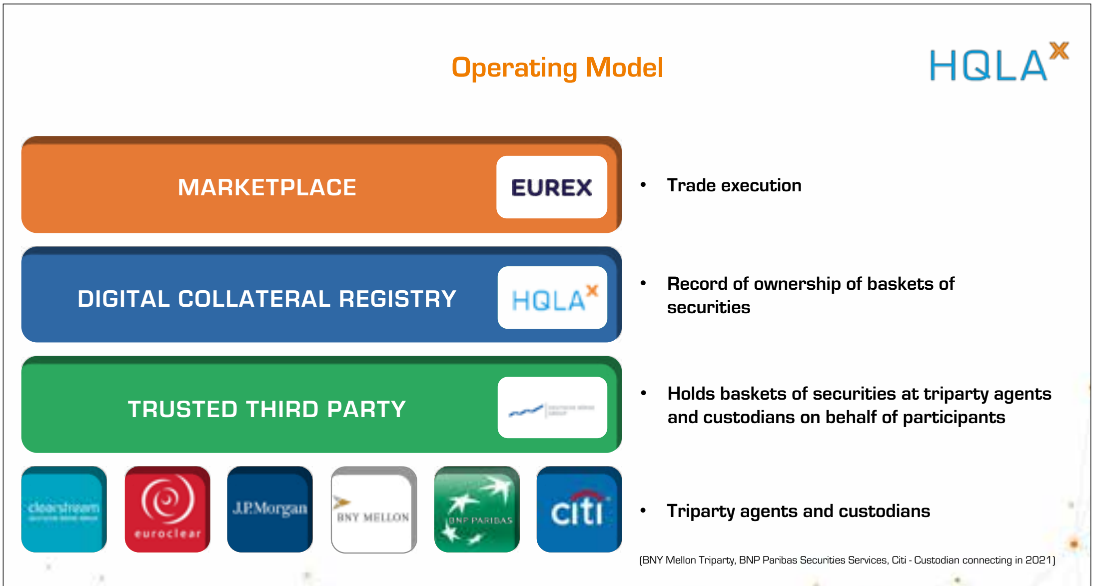
HQLAx operates a digital collateral registry: a blockchain-encoded set of ownership records. Below it sits the existing custody and settlement infrastructure – namely Clearstream, Euroclear and JP Morgan.

BNY Mellon, BNP Paribas and Citi will connect later this year, meaning the lion's share of European collateral is covered. Above it sits the market place on which execution occurs.

With each of the six tri-party agents and custodians plugged into HQLAx, a transfer of ownership is recorded in real time on the blockchain record, without any need to change the settlement location of the securities. That means no settlement process. And no delay.

Exactly what the delay might be depends on which of the 40-or-so CSDs in Europe is housing the securities. In this cat's cradle of infrastructures, a legacy of the national silos that traditionally controlled the settlement process, moving a security from one CSD can easily take one or two days.

The ownership transfer is both immediate and simultaneous. So it removes the intraday credit exposure inherent in Free of Payment deliveries – where the party who goes first has a credit exposure until the second party completes – and the balance intraday liquidity requirement inherent in Delivery versus Payment – where intra-day cash positions consume liquidity.



This gives users the ability to move [securities] around more freely, meaning they don't have to build in the scenarios in which it is delayed.

– Nick Short, HQLAx's chief operating officer.

Without the need for settlement, the instantaneous transfer of ownership allows banks to cut back the buffers used to protect against delays. "This gives users the ability to move [securities] around more freely, meaning they don't have to build in the scenarios in which it is delayed," says Nick Short, HQLAx's chief operating officer.

As well as reducing credit exposures and liquidity requirements intraday, HQLAx also reduces the operational risk from fails. Because as long as the basket is pre-collateralised, a fail is impossible. In future, this digital ownership record will be good for onward trades: the basket of securities provided by bank A to bank B can be employed in a subsequent trade between bank B and bank C with the same guarantee against failure.

HQLAx is reluctant to attach a number to the cash it can save its initial set of clients as it establishes its platform in Europe. But Oliver Wyman estimates that 10% - 30% of bank's HQLA buffer requirements are driven by intraday liquidity needs, and that proactive management of intraday liquidity can lead to sizeable reductions in a bank's intraday liquidity requirements of up to 25%. It estimates that every €1bn of HQLA costs banks roughly €10m in lost opportunity costs per year to hold. There is clearly a decent chunk of change to be saved.

4. Exploring distributed ledger in securities finance: OCC

Elsewhere, DLT is being used to support derivatives central counterparty clearing and settlement services by Chicago-based clearing house Options Clearing Corporation (OCC), in a new platform could begin testing as early as next year.

While not yet live, with $132bn worth of securities lending transactions the platform is likely to be one of the world's largest enterprise-wide applications of DLT when it launches.

Matthew Wolfe, Executive Director for securities finance at OCC, says that DLT is particularly well suited to the detailed bilateral nature of stock loans. "DLT allows users to track a securities lending transaction through all its steps through the entire life-cycle via a single immutable ledger. Transaction activity as well as the state of the contracts – current and historical – can be seen by parties that have adopted a node which allows them to monitor the shared ledger."

With OCC able to check details from the lender and the borrower align, errors will be identified before, rather than after the fact. "It means that OCC has full contract details allowing for more complete novation. And the

“DLT allows users to track a securities lending transaction through all its steps through the entire life-cycle via a single immutable ledger. Transaction activity as well as the state of the contracts – current and historical – can be seen by parties that have adopted a node which allows them to monitor the shared ledger.”

– Matthew Wolfe, Executive Director for securities finance at OCC

new system must handle a wider variety of life-cycle events including changes to rebate rates, recalls and buy-ins,” he says.

In early demos with a sample of OCC clearing and non-clearing members, users said that they were very supportive of the new system and highly likely to adopt it. Some said they would adopt the technology immediately; others said they were likely to start using the information provided by the ledger to compare with their existing records.

Harnessing Gains

The existing solutions from SmartStream, FIS Global and HQLAx are already improving efficiencies for securities lending participants, with the impacts flowing through the bottom line. And early signals from the OCC DLT-enabled platform are that users are aware of the difference it can make.

But adoption of AI and DLT solutions would benefit considerably from co-ordinated industry efforts, which remain fixed on prioritising standardisation.

“Distributed ledger technology (DLT), blockchain, and the tokenisation of collateral are second-order opportunities that could exist for the securities lending market once the foundations of digital standardisation have been laid,” wrote Citi’s Philip Winter, current Chair of the ISLA Digital Steering Group titled, in a March paper published by ISLA and Linklaters.

This could soon change. ISLA’s Common Domain Model, which will offer a template for transaction events allowing trade and other key information to be shared using a standard set of fields, is close to completion. Its Clause Library & Taxonomy for the core Global Master Securities Lending Agreement (GMSLA) is due to complete later this year. With these bolted down, innovation is likely to follow fast. ■

Three more applications of DLT and AI.

In December JP Morgan completed a live intraday repo transaction between its broker-dealer and banking entity, using an in-house developed blockchain application which supported instantaneous settlement. The transaction was completed in hours and the solution will soon see a commercial launch, with speedier execution helping reduce intraday risk.

In January Zürcher Kantonalbank and Deutsche Boerse’s post-trade services provider Clearstream processed their first live blockchain-based end-to-end fund transactions, using FundsDLT, a decentralised platform for fund transaction processing.

Elsewhere machine learning is being applied to reading and processing legal data. In January Delta Capita adopted the Luminance AI platform, already popular for accounting firms, to help it transition to alternative risk-free benchmark rates from LIBOR and IBOR, a process due to complete later this year.

The progression of ESG and the different routes to market within America's securities lending


Don D'Eramo, managing director and global head of securities finance and **Kyle Kolasingh,** associate director of securities finance at RBC Investor & Treasury Services (RBC I&TS) discuss recent trends in the Americas securities lending market such as ESG, specifically governance, and the increased focus of accessibility found within multiple routes to market.

Growing interest in ESG among beneficial owners and borrowers is a key trend across the global securities finance industry. In North America, the Securities Industry and Financial Markets Association (SIFMA) has noted that environmental, social and governance considerations are increasingly shaping the way investors choose to engage with companies and thus how companies do business.

"If you think of how one of the main aspects of ESG – governance – has been managed within the lending industry over more than a decade, it has been to recall or reallocate the security and free the loan position," explains Kyle Kolasingh. The ability to facilitate proxy voting and a well-functioning securities lending programme has not changed. We are however seeing more of this activity and having wider discussions on integrating such mandates into lending programmes as clients are looking into their overall governance strategy as part of their investment guidelines," he continues. "In the past, a higher number of clients would have selectively chosen which securities to vote, whereas now clients are considering what the next step looks like and how to integrate a wide-ranging proxy mandate with their agent lender to monitor securities and integrate that into their overall ESG strategy."

RBC I&TS has had this mechanism in place for some time and continues to monitor securities in its clients' lending programmes for those who want to proactively recall assets ahead of proxy dates. It also has regular discussions with clients to make sure the lending programme is compatible with the client's overall investment strategy. In this context, governance is not the only significant factor since there are other considerations, such as collateral. "We are also having more in-depth discussions on how

> **"Securities lending has always appeared to be a pretty straightforward industry on the surface, but the complexity comes from having to manage varying client goals."**
>
> **– Don D'Eramo**

> **“This business is complex even without ESG overlays. However, the strategy is always dictated by the underlying client, whether that is divesting from certain sectors or restricting certain sectors of collateral.”**
>
> **– Don D’Eramo**

short-term views fit in with ESG considerations and the association between securities lending and short selling,” says Don D’Eramo. “These conversations need to continue to evolve if liquidity is not to be hindered.”

The extent to which ESG considerations are integrated into the management of securities lending depends on how each beneficial owner has applied them from their investment strategy. From an RBC I&TS perspective it is about ensuring that beneficial owners achieve portfolio optimisation from their securities lending programme and maintain ESG compliance. “This business is complex even without ESG overlays. However, the strategy is always dictated by the underlying client, whether that is divesting from certain sectors or restricting certain sectors of collateral,” says D’Eramo. “Securities lending has always appeared to be a pretty straightforward industry on the surface, but the complexity comes from having to manage varying client goals,” he adds.

It has been suggested that the events of 2020 have underlined the importance of allowing clients to transact on a cash as well as a non-cash collateral basis. D’Eramo acknowledges that there was a flight to quality in the early stages of the pandemic, but suggests the collateral issues need to be looked at from a regional perspective. “In Canada, for example, the balance between cash and non-cash collateral has not changed in favour of the former over the last 12 months,” he says. “The US is still a predominantly cash market but reinvestment opportunities have presented some challenges given the situation with rates. There are some regulatory prohibitions around non-cash growth in the US which if removed would probably lead to increased use of non-cash collateral.” D’Eramo notes that Europe falls somewhere in between with a slight bias towards non-cash collateral.

“Overall we have seen increased demand for non-cash collateral from our counterparties in terms of ETFs, equities and term,” he adds. “Term went away somewhat as central banks introduced a lot of liquidity into the system but has started to return, albeit slowly.”

Another topic that has generated debate is the use of third-party agency lending by institutions and asset managers. “If you look at an agent lender such as RBC I&TS that has product capabilities across multiple client types and sectors (e.g., UCITS, pensions, sovereign/government institutions, insurance and asset managers), you have a very robust offering and the ability to provide a route to market that conforms to what clients want,” explains D’Eramo. “There are a few market participants who specialise in this type of lending (i.e., third party) in a concentrated way, for example, focusing on asset class transactions that are very narrow in scope,” he adds. “This may present opportunities in certain segments of the market.”

The decision to use a third-party agency offering often comes down to how the underlying beneficial owner sees their goals. For example, there may be large sovereign wealth funds with multiple providers who are not always their custodian. These funds may use multiple providers as an opportunity to diversify or even compare performance with the aim to achieve a best-in-market outcome. “The asset servicing discussion will span

Investor &
Treasury Services

Optimizing portfolio performance

For over 35 years, RBC Investor & Treasury Services' industry-leading securities finance program has been helping clients generate incremental returns through our trusted market expertise and established risk management framework.

#1 Income Generated*

To find out how our team of specialists can deliver a securities finance program that meets your risk and return objectives, visit rbcits.com.

*Global Investor/ISF Beneficial Owners Survey - Custodial Lender Category Unweighted, 2021

© Copyright Royal Bank of Canada 2021. RBC Investor & Treasury Services™ is a global brand name and is part of Royal Bank of Canada. RBC Investor & Treasury Services operates primarily through the following companies: Royal Bank of Canada, RBC Investor Services Trust and RBC Investor Services Bank S.A., and their branches and affiliates. In Luxembourg, RBC Investor Services Bank S.A. is authorized, supervised and regulated by the Commission de Surveillance du Secteur Financier (CSSF), and jointly supervised by the European Central Bank (ECB). In the United Kingdom (UK), RBC Investor & Treasury Services operates through RBC Investor Services Trust, London Branch and Royal Bank of Canada, London Branch, authorized and regulated by the Office of the Superintendent of Financial Institutions of Canada. Authorized by the Prudential Regulation Authority. Subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available on request. RBC Investor & Treasury Services UK also operates through RBC Europe Limited, authorized by the Prudential Regulation Authority, and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. Additionally, RBC Investor & Treasury Services' trustee and depositary services are provided through RBC Investor Services Bank S.A., London Branch, authorized by the CSSF and ECB, and subject to limited regulation by the Financial Conduct Authority and Prudential Regulation Authority. Details about the extent of our regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available on request. RBC Investor Services Bank S.A. maintains a representative office supervised by the Federal Reserve Bank of New York. RBC Investor Services Trust (Australian Branch) is licensed and regulated by the Australian Securities and Investment Commission, Australian Financial Services licence number 295018. Details about the extent of our regulation by the Australian Securities and Investment Commission are available on request. RBC Investor Services Trust Singapore Limited is licensed by the Monetary Authority of Singapore (MAS) as a Licensed Trust Company under the Trust Companies Act and approved by MAS to act as a trustee of collective investment schemes authorized under S286 of the Securities and Futures Act. RBC Investor Services Trust Singapore Limited is also a Capital Markets Services Licence Holder issued by MAS under the Securities and Futures Act in connection with its activities of acting as a custodian. RBC Offshore Fund Managers Limited is regulated by the Guernsey Financial Services Commission in the conduct of investment business. Registered company number 8494. RBC Fund Administration (CI) Limited is regulated by the Jersey Financial Services Commission in the conduct of fund services and trust company business in Jersey. Registered company number 52624. RBC Investor Services Bank S.A. is a restricted license bank authorized by the Hong Kong Monetary Authority to carry on certain banking business in Hong Kong. RBC Investor Services Trust Hong Kong Limited is regulated by the Mandatory Provident Fund Schemes Authority as an approved trustee. Royal Bank of Canada, Hong Kong Branch, is regulated by the Hong Kong Monetary Authority and the Securities and Futures Commission. This material provides information on the services and capabilities of RBC Investor & Treasury Services. It does not constitute an offer, invitation or inducement with respect to any service or financial instrument. RBC Investor & Treasury Services' services are only offered in the jurisdictions where they may be lawfully offered and are subject to the terms of applicable agreements. This material is for general information only and does not constitute financial, tax, legal or accounting advice, and should not be relied upon in that regard. ® / ™ Trademarks of Royal Bank of Canada. Used under licence.

"Agent lenders who can offer multiple routes to market by facilitating both the custodial and non-custodial lending are attractive to such beneficial owners as it allows for multi-model securities lending programmes to exist, allowing diversified optimisation of one's lending portfolio."

– Kyle Kolasingh

multiple disciplines, which makes this space more challenging," says D'Eramo. "There is room for third-party lending, but it is not the most significant part of the market."

Kolasingh agrees that this type of lending tends to take place in concentrated portfolios where the operational nuances are different from custodial lending. "Sophisticated beneficial owners of scale - typically government institutions - continue to assess what is best in class for these highly concentrated portfolios and third-party lending is gaining some traction in this space," he says. "Agent lenders who can offer multiple routes to market by facilitating both the custodial and non-custodial lending are attractive to such beneficial owners as it allows for multi-model securities lending programmes to exist, allowing diversified optimisation of one's lending portfolio." adds Kolasingh.

Over recent years, the securities finance industry has seen the introduction of various initiatives designed to make the market more accessible, including peer-to-peer lending. So what are the implications of this 'democratisation' of the market for agent lenders?

"The retail investor segment has been growing, but not as fast as might have been expected," says Kolasingh. "Expansion into different supply pools has been ongoing for a while and we have offerings where we show opportunities to clients that are not in lending to be able to participate in this market where we feel value is available." There are dealers in the US that have margin securities for other clients and make these available for loan. This business continues to develop and has co-existed with the broader institutional lending paradigms. "I see this continuing but I am not sure it is revealing anything about the retail space that was previously unknown," adds Kolasingh. The governing body for broker dealers in Canada has looked at creating guidelines for retail client assets to ensure there is an understanding of the risks and the market.

"This business is targeting intrinsic value securities, so if conviction continues to return to the market and we see more directional demand, supply will be borne out of that," says D'Eramo. "However, what is equally important is not so much the ability of this business to co-exist with agency lending but rather the fact that agency lending is regulated, highly transparent for clients and capable of being bespoke based on client requirements. When you move into the retail space, I am not sure if all these characteristics are present yet and regulators will potentially want to understand how these issues are addressed as the market for lending retail equities matures," he adds.

D'Eramo refers to peer-to-peer groups engaging in discussions around market practices as a healthy development for the market. "Over the past 18 months, we have created solutions for clients who want to gain leverage or run certain types of investment strategies where securities lending can be part of the solution. We expect that this peer space will continue to grow," he concludes. ■

One Year Old: Global Peer Financing Association

Global Peer Financing Association (GPFA) reflects on significant growth amongst large global beneficial owner members. Responses provided by **Jerry May,** Senior Portfolio Manager for Cash and Securities Lending with OPERS and GPFA Board Member

"This inaugural year has been challenging and rewarding on several fronts. We've been able to consistently draw upon members' expertise to provide education to beneficial owners, while amid a global pandemic."

July 2021 marks the one-year anniversary of the founding of the Global Peer Financing Association (GPFA). What challenges has the association faced?

Thank you. This inaugural year has been challenging and rewarding on several fronts. We've been able to consistently draw upon members' expertise to provide education to beneficial owners, while amid a global pandemic. It's been disappointing that we have not been able to gather collectively to share thoughts and information, but we have adapted as everyone else to the new virtual meetings and have been able to incorporate those offerings in our communication and membership engagements. It's been great to see how much participation we are seeing in those discussions on a regular basis.

What has the GPFA accomplished this year?

From our beginnings with just four founding beneficial owners being HOOPP, CalPERS, OPERS and SWIB, with assets of just under $1 trillion, the association has now grown to almost 20 members, with assets pushing $7 trillion. There has been a consistent exchange of information about various industry topics, educational seminars to discuss approaches to operational and financial issues that different member organisations employ, a regular podcast that provides thoughts on relevant industry topics, and a network of like-minded peers who are able to ask and

> **The participation within the member organisations has also grown beyond simply the managers of the securities finance or repo departments, to include other areas of the firms, such as corporate governance, technology, and management.**

answer questions about issues with which the buy-side must wrestle. It's been a challenging environment to begin an association, but word of mouth has been strongly positive, and members enjoy the forums that have been provided for discussions. One of the most rewarding aspects of this first year has been to see how involved our members have been in leading conversations for beneficial owners that had previously been relegated to infrequent conferences. Members such as Norges Bank, CDPQ, CPPIB, AustralianSuper and CalSTRS, just to name a few, have all provided leadership in this area. The participation within the member organisations has also grown beyond simply the managers of the securities finance or repo departments, to include other areas of the firms, such as corporate governance, technology, and management.

What has the reception been like in the industry?

The GPFA has been able to communicate its message that the securities finance industry is much larger than many might believe. There are opportunities in the industry for doing things in many ways, and the plethora of approaches by members provides a great way for everyone to learn something new. Peer-to-peer financing is but one aspect of that opportunity set. As beneficial owners seek to add alpha to their plans, especially in low interest rate environments like the one we are experiencing globally now, each basis point becomes valuable. Beneficial owners that want to utilise securities lending or repo as tools for liquidity facilities, collateral management or leverage are finding opportunities with peers when their traditional trading counterparts are often otherwise limited by regulatory constraints or capital requirements.

Diversifying trading approaches, counterparties, and investment themes only makes sense to owners who wish to maximize portfolio returns. GPFA has been happy to engage with other industry organisations and thought leaders to help make that a reality for our members. The association has received well wishes and offers of assistance from many market participants, and we suspect that everyone who is active in this sector would appreciate a more engaged and educated principle or end buy-side client.

> **The reception of the content offerings provided by GPFA for current and potential members has been wonderful. The networking and social media interaction continues to be very active. Inquiries from buy-side accounts on new membership are frequent.**

Have there been any surprises from this first year?

When the founding members initially began discussions to formalise the association, there was not a roadmap of similar institutions to

“The association very much looks forward to a hopefully not-too-distant future where we can once again physically get together, interact and exchange information and we are currently targeting our annual in-person meeting in the spring of 2022.”

follow. The work to build the association has been thoughtful, but with little guaranteed in the way of success. Thankfully, the results have been very positive, and demand has been very strong for what the GPFA has created for the buy-side beneficial owner community in securities finance. The reception of the content offerings provided by GPFA for current and potential members has been wonderful. The networking and social media interaction continues to be very active. Inquiries from buy-side accounts on new membership are frequent. The experience of the founding members in starting an industry association such as GPFA one could say was relatively ‘thin’. Yet, the reception of GPFA has exceeded all expectations, and that is a testament to the demand for this type of organisation by beneficial owners, and the responsiveness of the GPFA leadership in adapting strategy to meet expressed concerns and needs of the members.

The surprise, one might say, is in how well-received the GPFA has been from the asset owners that we hope to serve. There is an appetite for timely discussions of issues that are occurring in real-time. There has been a very substantial transfer of knowledge and information across the participant base, and that has been a great thing to witness. Growth has been substantive, and steady, and that has been a real benefit. Our partner companies have been ideal in working with the association and its members. Without those partners, the GPFA would never have been able to see the impressive growth it has.

What are the plans for this next year?

One could very easily say in many respects it will be more of the same. The GPFA will continue its educational offerings, social media interactions, and regular discussions with and for its members. There will continue to be engagement with other industry groups and organisations for the benefit of the buy-side. We anticipate continued growth in membership across the larger beneficial owners engaged in the securities financing markets. The association very much looks forward to a hopefully not-too-distant future where we can once again physically get together, interact and exchange information and we are currently targeting our annual in-person meeting in the spring of 2022. Our members are getting to know each other well virtually but we are confident the group will benefit from spending time together in person next year.

There is also an awareness on the part of the board that the organisation can have a broader impact than merely within securities finance, although that is the foundation upon which the group was founded and will always be primarily concerned. It would be short-sighted to ignore how the benefits of interacting with like-minded peers could also provide value to member organisations in larger contexts. Longer-term, we have seen and experienced the benefits of this interaction in the securities finance area and have come to realise the connections between member organisations across other functional areas and investment disciplines could similarly assist in enhancing member value. ■

Rethinking the investment process

Vikas Nigam, director, head of Americas for agency securities lending at Deutsche Bank outlines the development of the bank's US business and the diversification of use cases in this significant market.

When global markets plunged in March 2020, many Deutsche Bank clients in the US - particularly state treasurers and state pension funds - feared that with lower tax revenues and increased healthcare and employment costs, they would face a liquidity squeeze.

"We provide a high touch service resulting in deep client engagement," says Nigam. "So when Covid first hit, our clients naturally engaged with us to see how best to unlock liquidity from their securities lending portfolio as an alternative to an outright sale. However, when policy makers stepped in with monetary and fiscal measures, some clients found themselves with the opposite problem of having to manage an excess of liquidity."

This created issues around low yields and a lack of investment returns, which led to an increased focus on securities lending as a way of driving the incremental return clients need. With so much cash in the market from money funds in particular, there was a lack of investment options and repo collateral available.

In light of this opportunity and reflecting the ongoing diversification of use cases, Deutsche Bank moved its securities lending business across to the cash management arm of the bank.

"We rethought the investment process from the ground up to deliver a front to bank investment process to clients to invest their excess cash in our reverse repo and money market offerings," says Nigam. "Not only was this available to our existing securities lending clients, but with our realignment to cash management we are also expanding our reach to a much larger client base."

Another way the bank differentiates itself is by maintaining a proactive approach to market and regulatory developments. "A good example of this is the recent implementation of the net stable funding ratio (NSFR) by broker dealers globally, which has resulted in newer trade structures in the market," explains Nigam. "This allows us to engage with our clients around the expansion of guidelines to make their portfolios more attractive."

"Flexibility is really going to be a key theme over the next 18 months," he adds. "Clients will need to be flexible to adapt and help counterparties become more efficient from a regulatory standpoint. Counterparties will need to be flexible as clients shift attention and focus to embedding ESG into their investing and securities lending process."

According to Nigam, that level of engagement is going to be there for as long as clients want it. "We appreciate that not all clients have the bandwidth to focus on securities lending to the extent that they might want to and while they are engaged and wanting to talk to us we are happy to keep talking to them about all the things we are seeing."

In terms of use case diversification, an obvious example is tapping the cash collateral pool as a way of helping fund other needs. Deutsche Bank is currently engaging with a client that is looking to monetise its treasury portfolio under a term structure, prioritising liquidity management over revenue generation.

"Another use case is where investment managers are adapting their investment strategy based on the additional revenue they are able to earn from securities lending," says Nigam. "They are now using securities lending revenue as an added input into their portfolio selection and construction and using us as an agent to help price and generate alpha for their client."

As an example, clients can choose to buy a TIP with a higher yield and lower associated securities lending revenue or a Treasury Bill with a lower yield but a higher securities lending return based upon their near 100% demand from a securities lending prospective. The same applies to equities, where clients have to decide whether to go for a swap or hold the equity and have securities lending revenue attached to that.

Deutsche Bank has clients in a number of

"Clients will need to be flexible to adapt and help counterparties become more efficient from a regulatory standpoint. Counterparties will need to be flexible as clients shift attention and focus to embedding ESG into their investing and securities lending process."

> **Many of the largest ETF and mutual fund providers as well as pension funds in the US have committed to non-custodial securities lending solutions.**

different segments from asset managers to insurance companies and pension funds, but its US business is predominantly public funds.

"This is pleasing for a number of reasons," observes Nigam. "Public entities have some of the most stringent and transparent selection criteria, so we are obviously doing something right for them to choose us. Secondly, Deutsche Bank isn't a household name compared to some of our US peers so for these entities to feel comfortable enough with us to select and push for us with their boards over a household name shows the level of confidence we have generated. That in itself is an incredibly powerful endorsement."

"Clients have stayed with us throughout our transformation journey and now that we are on a much stronger footing we are growing our mandates with them," he adds. "They are giving us additional assets or widening their guidelines with us and we are looking to sell to more clients and expand our offering."

The investment in the securities lending programme in terms of technology has been a crucial factor in giving Deutsche Bank a larger client base to potentially cross-sell to. It is also indicative of an understanding and a strategic view on agency securities lending from the bank's franchise in the US.

"We are a very efficient product for the bank as well as our clients, so it makes sense they would use us and continue to focus on us," says Nigam.

Deutsche Bank has previously referred to the trend for some of the largest institutional investors in the world to separate custody or securities services from lending.

"The decoupling of custody from securities lending has been going on in the US for more than a decade now," explains Nigam. "Many of the largest ETF and mutual fund providers as well as pension funds in the US have committed to non-custodial securities lending solutions. These include Blackrock, Fidelity, Janus Henderson and two big Californian pension systems, to name just a few"

A number of custody platforms have also set up their own third party lending agents in an attempt to capture some of this market given clients' growing preference for such a model.

"I think this trend will continue - custody platforms are trying to fight back by reducing custody fees where clients maintain their securities lending with them as well," says Nigam. "It is also dependent on the client's priorities. You want to go for the best in class and a pure third party lending agent is focused on service, revenue and risk, whereas a custody platform doesn't necessarily have the same focus on the securities lending part of their offering."

He observes that Deutsche Bank's clients have had to make a conscious decision to decouple securities lending from custody and the fact that they haven't gone back is a testament to their satisfaction with this decision.

"Some clients don't want to engage too much with securities lending and are happy to leave it to the custody platform to do that," concludes Nigam. "Other clients see securities lending as a real opportunity to make that incremental revenue and really want to maximise it within risk managed boundaries and are looking for third party agents to do that for them." ■


Deutsche Bank
Corporate Bank
Optimise opportunities
#PositiveImpact
Deutsche Bank offers comprehensive market coverage and operational efficiency for institutional investors and treasurers seeking access to securities lending and repo markets.
Working with Deutsche Bank, you not only benefit from our market-leading insights into an ever-changing environment, but also from powerful infrastructure, innovative technology and integrated solutions – helping you optimise every securities lending and liquidity management opportunity.
For more information call our Agency Securities Lending team in London on +44 20 754 75225 or email maurice.leo@db.com or in New York on +1 212 250-4492 or email joseph.santoro@db.com.
Follow us on twitter @DBCorporateBank
This advert is for information purposes only on a non-reliance basis and is designed to serve as a general overview and to provide information on certain services of Deutsche Bank AG, any of its branches and affiliates. This advert does not create any legally binding obligations on the part of Deutsche Bank AG and/or its affiliates ("DB"). Without limitation, this advert does not constitute an offer, an invitation to offer or a recommendation to enter into any transaction. This advert does not constitute the provision of investment advice and is not intended to do so, but is intended to be general information. The general description in this advert and the services offered by Deutsche Bank AG, any of its branches and affiliates ("DB") to customers may be subjected to change without notice. The information contained in this advert is based on material we believe to be reliable; however, we do not represent that it is accurate, current, complete, or error free. DB has no obligation to update, modify or amend this advert or to otherwise notify a recipient thereof if any opinion, forecast or estimate set forth herein changes or subsequently becomes inaccurate. Any product(s) mentioned herein may not be appropriate for all investors and before entering into any transaction you should take steps to ensure that you fully understand the transaction and have made an independent assessment of the appropriateness of the transaction in the light of your own objectives, needs and circumstances, including the possible risks and benefits of entering into such transaction. For general information regarding the nature and risks of the proposed transaction and types of financial instruments please go to https://www.db.com/legal-resources under the heading "Risk Disclosures". The distribution of this advert and availability of these products and services in certain jurisdictions may be restricted by law. You may not distribute this advert, in whole or in part, without our express written permission. DB SPECIFICALLY DISCLAIMS ALL LIABILITY FOR ANY DIRECT, INDIRECT CONSEQUENTIAL OR OTHER LOSSES OR DAMAGES INCLUDING, BUT NOT LIMITED TO, LOSS OF PROFITS INCURRED BY YOU OR ANY THIRD PARTY THAT MAY ARISE FROM ANY RELIANCE ON THIS ADVERT OR FOR THE RELIABILITY, ACCURACY, COMPLETENESS OR TIMELINESS THEREOF. Deutsche Bank AG is authorised under German Banking Law (competent authorities: European Central Bank and German Federal Financial Supervisory Authority (BaFin)) and, in the United Kingdom, by the Prudential Regulation Authority. It is subject to supervision by the European Central Bank and the BaFin, and to limited supervision in the United Kingdom by the Prudential Regulation Authority and the Financial Conduct Authority. Details about the extent of our authorisation and supervision by these authorities are available on request. Copyright© April 2021 Deutsche Bank AG. All rights reserved.

Women in Securities Finance finds strength in numbers

Elaina Benfield, Arianne Collette, Jill Rathgeber.
Co-Founders and Global Tri-Chairs of Women in Securities Finance



What has Women in Securities Finance been able to accomplish in 2021?

Website: In late March, we announced the launch of the Women in Securities Finance (WISF) website, which provides information about the group/mission, upcoming events, podcasts and featured articles. Those interested in becoming a member are now able to join through the website and be a part of the 600+ member group, representing more than 80 organisations across the industry.

Quarterly Newsletters, Social Media Presence, and Featured Interviews: We anticipated this remote environment for the better part of the year, so we wanted to ensure we were able to reach our members in a variety of ways. The quarterly newsletters were designed to provide industry updates, highlight upcoming events, and feature news about our members. WISF also expanded its social media presence by creating a public profile on LinkedIn to reach a broader audience than just the members of the group. Finally, in the private WISF LinkedIn group, which is open to anyone to join, we have encouraged members to share job postings and opportunities within their firms, thereby helping to promote opportunities directly to the members of the group.

Podcast Series: The end of last year, we launched a monthly podcast series, Perspectives by Women in Securities Finance, which is a platform for WISF and its allies to discuss issues impacting the industry, topics related to professional development and diversity, equity and inclusion. We've published 9 podcasts, had over 1,500 downloads since inception and have many more exciting and informative podcasts scheduled for release this year.

Diversity, Equity and Inclusion: Our London Chapter leads collaborated closely with the Bank of England to incorporate diversity, equity and inclusion standards in the UK Money Market Code and highlighted the need for firms to prioritise, and focus on inclusion more as they start incorporating new working models into their organisations.

Virtual Networking events: The Toronto chapter has hosted two virtual events this year, which were open to all members. Both sessions featured senior female executive leaders in their (non-financial) industries speaking to effective leadership, challenges faced while climbing the corporate ladder, and lessons learned.

In summary, the first half of 2021 has been very productive for Women in Securities Finance. All of these accomplishments have helped to further our mission of keeping the community connected and promoting diversity, inclusion and the advancement of women in the securities finance industry.

Following the launch of the London Chapter in 2020, is WISF looking to launch elsewhere?

We continue to thoughtfully consider expansion of the group, both geographically and strategically. From a geographical perspective, Asia would naturally be the next step; however, we need to balance our expansion strategy with making sure we continue to further the mission and strengthen the brand. Given the breadth of the APAC region, time zone challenges and the fact that we are predominantly still in a remote environment, we decided it would be best to first collaborate with peer groups and members in region, to increase awareness of Women in Securities Finance and establish the needs and goals of those locally.

From a strategic perspective, we are considering collaborations with other established groups in the financial services industry to bring fresh ideas and programming to our members. Lastly, as we return to work, we are exploring adding a philanthropic partnership to programming.

How are you still engaging with your members and what are you hearing from them?

The current environment has made it more difficult for some, especially new members, to make connections within the industry. With that in mind, we made a conscious decision to find more ways to communicate with and connect to our members. As we mentioned earlier, the website, podcasts and quarterly newsletters have helped to inform and educate, but we've also offered opportunities to connect in smaller groups. Both our Chicago and Boston chapters have held smaller virtual networking events in the first half of the year and we are currently scheduling additional sessions in an effort to allow members to make new connections, re-establish former connections and share our individual career journeys and experiences. Finally, we plan to send out a survey to all members, in an effort to obtain additional feedback regarding the impact of WISF and ideas for how to best carry out our mission and achieve our goals in the future.

What message would you like to leave your members?

We encourage all members to actively participate by sharing their ideas and suggestions for advancing the group's mission and delivering programming that is valuable, educational and relevant. We are mindful that different members have different needs with respect to what they seek from the group, so we encourage all to share their thoughts with any of our chapter leads.

We are hopeful that as firms return to the office, it will create opportunities for our members to participate in in-person events. While we are looking forward to those opportunities, we must also recognise that, similar to the challenges we all faced shifting to a fully remote workplace, the return to office may be equally as challenging. We have all spent over a year and a half adjusting and adapting our lives as a result of the pandemic, and now we find ourselves having to do it all again. We urge members to leverage the WISF community; listen and support each other as we navigate these challenges together.

Finally, we want to sincerely thank all our members for their efforts, support and participation this year, as well as the firms who have sponsored events and supported WISF in furthering its mission. We look forward to continuing to connect and engage with you in the future. ■

Securities lending in a changing world

Bill Kelly, global head of agency securities finance at BNY Mellon considers what recent high-profile defaults and the rapid emergence of meme stock trading mean for securities lending, and reviews recent progress towards regulatory compliance by the industry.

How did the recent events related to Wirecard and Archegos impact the securities lending industry?

These two events brought about a renewed focus on securities lending and the role it plays in facilitating short selling. This re-ignited familiar debates with respect to short selling and its part in maintaining efficient markets, promoting liquidity, aiding price discovery, and exposing corporate irregularities

Last summer, Wirecard highlighted the role short-sellers play in disseminating information. Their early alarms provided the first indications of malfeasance at the company and they can reasonably claim to have demonstrated their usefulness in promoting market transparency.

More recently, the Archegos default has increased attention on short positions established through the use of synthetics. Synthetic structures allow considerable short exposure to build up unseen, in contrast to when the same views are expressed through conventional transactions. The point has been made several times that, had Archegos expressed its views through physical short sales supported by borrowing the securities from agent lenders, it would have faced significant leverage limits that would have curtailed its exposure to a small fraction of what it eventually accumulated and may have averted its demise.

"Synthetic structures allow considerable short exposure to build up unseen, in contrast to when the same views are expressed through conventional transactions."

The lack of transparency with respect to synthetic short positions will no doubt be the focus of the post-mortem surrounding the Archegos event and the difficulties faced by its counterparties in liquidating positions in names that had suddenly become distressed. We are already beginning to see the regulatory response. FINRA recently issued Regulatory Notice 21-19 requesting comment on proposed enhancements to short interest and short sale reporting. Under the proposal, synthetic short positions would be included in short interest reporting along with customer borrows in arranged financing programs. In addition,

> **“We are early in the journey towards a greater understanding of how social media and individual investors can impact markets that have traditionally been the purview of institutional investors.”**

more granular reporting is being proposed that would require separating short interest between proprietary and customer positions as well as providing account level position reporting. Increasing the frequency of the reporting to either daily or weekly is another proposal. These proposals are likely the first step in addressing the limitations of short interest reporting which to date has been a lagging indicator and a fairly archaic signal when it comes to providing an early warning of problems. From a securities lending perspective increased transparency has been an ongoing theme since the 2008 financial crisis and was a central pillar of the work done by the Financial Stability Board which ultimately led to the SFTR reporting regime. I fully expect to see continued advancements in transparency especially as new technologies become available.

What consequences does the emergence of meme stock trading hold for securities lending?

Clearly it is early days in how the market and regulators treat the phenomenon of heightened market volatility involving stocks such as GameStop, Hertz or AMC. The phenomenon is clearly attracting close scrutiny – as demonstrated by the hearings held earlier this year by the US House Committee on Financial Services. Nevertheless, we are early in the journey towards a greater understanding of how social media and individual investors can impact markets that have traditionally been the purview of institutional investors.

Two things that are worth emphasising here. The first is that the market has without fail functioned efficiently through the price events surrounding these stocks. Clients could participate or withdraw from securities lending positions throughout the most severe periods of volatility. The second, which I think has been omitted from much of the coverage, is that we are seeing the democratization of securities lending with the rise of retail lending. Most retail brokers now provide retail clients with the ability to lend securities in their accounts and earn additional return.

What role do agent lenders have to play in smoothing the path towards regulatory compliance?

With the progress of the EU Securities Financing Transactions Regulation (SFTR) and its derivative equivalent under EMIR, it is clear that reporting regimes aimed at increasing transparency for securities financing will soon be adopted by other jurisdictions. Clearly, the documentation requirements of filling roughly 150 data fields as required by SFTR are considerable and hopefully the industry will be able to fashion sensible data exchanges to facilitate that process.

As the delegated reporting agent, it falls to us, in partnership with technology vendors, to deliver provide the required information to the data repositories. We recognize that this is a considerable responsibility and it is vital for us to reduce the associated burden. We must assist our asset owner clients on this journey so that they are still able to continue to earn additional alpha through their securities lending activities, while alleviating the regulatory friction for them.

By the same token it is clear that there is a benefit to providers of easing the transition through regulatory compliance for our clients.

“From an agent lender’s point of view, our clients are bringing liquidity to these platforms that provide resource efficiencies to their counterparties and therefore they should be paid a premium.”

If we simply said ‘here are the rules and obligations’ and left them to get on with it by themselves we know where that would lead. Clients don’t need to do securities lending; they are choosing to do it. If it becomes too hard for them, they will could opt out. We have a responsibility to support asset owners in this transition towards greater transparency.

What have you learned from the slow progress towards building a successful cleared securities lending solution?

Operating models that work in this area are those that are buy-side friendly, make economic sense for both the agent and its client, and are easy to adopt. Eurex was the first central counterparty to develop a workable clearing model that preserved the existing relationships of the bilateral agent lending market without imposing the traditional obligations of a clearing member on buy-side participants. We were fully committed to the Eurex product and disappointed that it closed. At the same time, we, like other participants, recognize new structures take time to establish through an iterative process of learning and refinement. We continue to work with Eurex on adapting their existing repo clearing products to make them viable solutions for our program.

The FICC Sponsored Member Program is another clearing model that we utilize within our agency lending program as an additional distribution channel for cash and US government securities. In addition, we continue to follow new developments being made on new models at NSCC and the OCC.

Generally speaking, we are learning that each new proposed model has limitations and challenges. One of the main challenges is the question of how default fund contributions and transaction costs are allocated. In addition, there is the question of documentation and how that shapes adoption. Broadly speaking, the easier the industry can make it for clients to participate, the quicker liquidity will arrive to the platform. Cleared transactions also need to be resource efficient for both the counterparties involved and for facilitators like us.

From an agent lender’s point of view, our clients are bringing liquidity to these platforms that provide resource efficiencies to their counterparties and therefore they should be paid a premium. Without that premium, it will be harder to justify the costs associated with clearing in many of these models. Making the economics work for all participants needs to be the goal if these models are to succeed.

“We have a responsibility to support asset owners in this transition towards greater transparency.”

What does the industry need to do to assimilate the growing emphasis on ESG compliance?

When it comes to ESG a process of some degree of standardization needs to take place. Standardization is a pre-requisite in order for a set of consistent principles and definitions to be established that asset owners can employ and which can be used as a blueprint for securities lending providers to follow, whilst at the same time allowing flexibility for

“Achieving standardization when it comes to scoring on these ESG factors measures is a process that will rely heavily on industry bodies on the one hand and regulators on the other.”

regional differences in regulatory frameworks and recognising the variation of transition pathways to sustainable outcomes

The question of governance has been around in securities finance for some time, such as issues around proxy voting and the other means by which clients have been able to exercise their stewardship responsibilities. The environmental and social dimensions will be those that we look to for progress in the future. Achieving standardization when it comes to scoring on these ESG factors is a process that will rely heavily on industry bodies on the one hand and regulators on the other. In order to achieve this, it will be important for ESG ratings to be reliable, transparent and comparable. But I am confident that the industry will soon deliver the principles required for an efficient operating model. These, in turn, will provide the level of transparency required by boards or senior management teams that allow them to demonstrate that they are fully aligned with their declared ESG principles and provide validation to the fact that securities lending is compatible with ESG and furthermore, can be a helpful tool in advancing the sustainable finance agenda.

How can providers help buy side clients achieve UMR compliance?

Phases 5 and 6 of UMR will bring into scope more than 1,000 new entities required to comply with margin requirements for uncleared derivatives. This will create considerable responsibilities for them, and they are looking to providers like us for solutions. The buy side will need a comparable set of utilities and solutions to those developed for the sell side – harnessing structures such as pledge. These have the potential to provide highly financial resource-efficient ways to address the compliance challenge.

But UMR is part of a wider shift toward increasing emphasis on transforming and optimising collateral across the entire enterprise. In some cases this will provide the buy-side with additional revenue opportunities by employing surplus HQLA or cash that is not immediately needed. Aggregating information and optimising these assets across the business provides a valuable way for a firm to meet its regulatory obligations as well as unlocking the revenue opportunities associated with assisting other counterparties.

As cleared transactions become another part of the opportunity set, it is important to remember that they may not be appropriate in all cases. Sometimes, they may not offer exactly the hedge that a client is after and an uncleared product may be more suitable. But importantly they will now have a clear choice concerning the venue and product best suited to their needs at that time. Armed with the tools and understanding we can supply, clients can make an informed choice between the cleared and uncleared derivative route, unencumbered by concerns of how efficiently the pre- or post-trade lifecycle of the trade will be managed. ■

“As cleared transactions become another part of the opportunity set, it is important to remember that they may not be appropriate in all cases.”

IHS Markit®

Analyze. Understand. Monitor.

Leverage our experience to optimize your program performance, enhance investment decisions, and confirm good governance through powerful tools and analytics.

- Largest securities lending dataset includes corporate actions, credit consensus, ETF collateral lists, liquidity and more
- Global securities lending flows, borrow costs and market share updated intraday
- Diverse signals to identify short squeezes, capture alpha, and refine risk management
- Robust performance measurement tools exceed enhanced industry standards
- Full-service governance, performance, risk, and operational assessments

Learn more at ihsmarkit.com/SecuritiesFinance

The global leader in securities finance solution

671560176_0721_CU

CONTACT US | MSF-Sales@ihsmarkit.com

NORTH AND SOUTH AMERICA	EUROPE, MIDDLE EAST AND AFRICA	ASIA PACIFIC	JAPAN
+1 800 447 2273	+44 1344 328 300	+604 291 3600	+81 3 6262 1887

Argentina

The Argentinian economy has been in turmoil since the south American country requested assistance from the International Monetary Fund in 2018.

Bolsas y Mercados Argentinos (BYMA), the stock exchange group, has been progressive in its approach to securities finance and incorporated in 2018 the "Short Sale" as a new type of operation, and updated the conditions of its "Securities Loan" definitions.

"Short-selling, in normal market conditions, plays an important role in ensuring financial markets function correctly, especially with regards to market liquidity and efficient price formation," the National Securities Commission (CNV) said at the time.

The exchange sees a securities finance market that follows the best international practices and regulations as a key building block in the country's attempt to be re-classified as an Emerging Market.

Short selling and securities loans must be carried out on the MILLENNIUM platform used by BYMA while the exchange also acts as a central counterpart, guaranteeing the settlement of these operations at the due date.

In the Argentine market, short selling can only be performed by local brokers provided that they borrow the shares from BYMA's securities lending program on trade date (three days prior to settlement date).

Custodial functions are undertaken by the Caja de Valores SA which acts as Central Depositary Agent for Negotiable Securities (ADCV) under the terms of the Capital Market Law.

In this capacity, Caja de Valores SA enters into a collective deposit agreement with each

“Short-selling, in normal market conditions, plays an important role in ensuring financial markets function correctly, especially with regards to market liquidity and efficient price formation.”

– the National Securities Commission (CNV)

Depositor, by which the depositor delivers to it a certain amount of negotiable securities, and Caja de Valores SA assumes the commitment to return the same amount of negotiable securities of the same kind and class.

The negotiable securities are deposited at the order of the Depositors and in the name of the Principal, who are the owners thereof. For these purposes, the Depositors are responsible for registering their clients (holders of the negotiable securities) through the opening of accounts called “Principal Sub-Accounts” and to which they are assigned an identification number.

Currently, almost all of the negotiable securities deposited in Caja de Valores SA are dematerialized or represented by global certificates.

Caja de Valores SA receives from the issuers the dividends, interest or any other credit to which the deposited negotiable securities give the right; proceeding to its accreditation in the client accounts and payment according to procedures established for that purpose and approved by the National Securities Commission.

Likewise, and within this scope, Caja de Valores SA offers its depositors the services of subscription of new issues, as well as the exercise of voluntary or mandatory exchanges.

In order for local investors to keep internationally issued negotiable securities in custody, Caja de Valores SA has accounts in the following Depositories: Euroclear, Clearstream, Iberclear, and in The Depository Trust Company.

In the case of Iberclear, the Depositary also has an account open as a Depositor of Caja de Valores SA, which allows Spanish investors to have Argentine securities deposited in the same.

Reciprocal accounts are enabled with the depository B3 (Brazil), which allow investors from both countries to carry out operations with securities on the Buenos Aires and São Paulo stock exchanges. ■

Argentina equities (US$)

	2019	2020	Q1 2020	Q1 2021
Securities lending revenues	$3,424,319	$1,893,416	$394,866	$684,280
Average loan balances	$840,981,641	$965,484,550	$745,579,318	$1,284,306,749

Source: IHS Markit

Brazil

Since the 2017 merger of Cetip and BM&FBovespa to form B3 (Brasil, Bolsa, Balcao), the Brazilian exchange group has been working hard to develop services for the securities lending market.

B3 delivered in 2019 new functionalities to support securities lending activities, including the introduction of securities lending services for government bonds, the automation of broker-dealer accounts and the creation of an electronic securities lending platform.

More recently, the Sao Paulo-based group introduced Circuit Breakers in March 2020 to counter the extreme equity trading volatility caused by the COVID-19 pandemic.

Under the current securities lending program, B3 acts as service manager and the central counterparty to all operations, adhering to risk control criteria and rules for the well-functioning of the market.

The securities lending activities are ruled by the registration of a loan agreement set through a voluntary loan between a borrower and a lender which regulates the mutual promises made by each party or a compulsory loan triggered under exceptional circumstances by B3 for borrowers that still have to count on the willingness of an available lender.

The securities eligible for securities lending transactions include shares issued by publicly-held companies authorized to trade at B3 and

As the industry grows and matures, Genesis LCAP provides the building blocks and agility to address the Brazilian market's very specific requirements across asset classes market trading infrastructure.

– Paulo D'Angelo, Managing Director at B3

other securities at the discretion of the B3 clearing house.

The securities involved in lending transactions must have been previously deposited with the clearing house's depository service. The securities must be free and clear of any liens or encumbrances that may restrict their circulation and their holders must have contractually consented to transactions of this kind.

Currently, eligible securities are: Stocks (authorized to trade on the stock market); Units (assets composed by more than one type or class of securities); Exchange-traded Funds (ETFs); Brazilian Depositary Receipts; Real Estate Investment Funds; and Equity Investment Funds.

The Brazilian stock exchange selected in December 2020 Genesis Low-Code Platform (LCAP) to deliver performant, resilient solutions to address multi-faceted highly complex post-trading workflows, securely at pace and at scale.

"We conducted a thorough market assessment on Low-Code Platforms, and Genesis emerged as the leading low-code firm, one that is uniquely designed for the standards of software development within financial markets. As the industry grows and matures, Genesis LCAP provides the building blocks and agility to address the Brazilian market's very specific requirements across asset classes market trading infrastructure," said Paulo D'Angelo, Managing Director at B3.

"Impressed by Genesis' low-code platform, we put it to work immediately. We set out a highly complex event processing Proof-of-Concept (PoC) involving stress-testing and handling high-frequency spikes in millions of trade messages. Genesis' low-code platform tackled and addressed the challenge in a matter of weeks. Based on this first PoC, we have every confidence that Genesis will be a key partner in helping us identify and deliver immediate and future opportunities for further efficiencies," added D'Angelo. ■

Brazil equities (US$)

	2019	2020	Q1 2020	Q1 2021
Securities lending revenues	$6,295,178	$3,223,867	$1,102,969	$843,051
Average loan balances	$379,912,618	$293,531,751	$284,987,418	$341,935,726

Source: IHS Markit

Canada

The Canadian equity lending market is the second largest in the region, but its recovery from the onset of the Covid-19 pandemic has been significantly slower than that of its larger neighbour, with revenues for the first quarter of 2021 down 54% year-on-year. Canada's equity lending market generated around $75 million between January and March this year, which is a significant drop compared to Q1 2020's $163 million. The market generated a total of $442 million in 2020, although at its current rate, it may struggle to achieve a similar figure this year.

Despite the drop in revenue, on-loan balances in the Canadian equity market increased in the first quarter of 2021. On-loan balances in the first part of the year were just over $40 billion, representing a 13% increase on last year's $36 billion. At the end of 2020, the value of Canadian equities on loan dipped slightly by around $100 million.

Early in 2021, the heightened volatility across the US equities market had a knock-on effect across Canada, with the nation's regulators quick to announce they were closely monitoring how extreme price movement in certain stocks may be contributing to the volatility in its capital markets. The Canadian Securities Administrators (CSA) and the Investment Industry Regulatory Organization of Canada (IIROC) were prepared to take regulatory action to protect investors if they identified abusive or manipulative trading activity is taking place. They said in February: "With strong market oversight and surveillance infrastructure in place, Canadian regulators are working together closely to protect investors while ensuring that the markets operate in an orderly manner and with integrity."

The two bodies worked closely with domestic and international regulators as they emphasised that trading and market

"In recent years, activist short selling campaigns have received considerably more attention, and stakeholders have raised concerns about the overall impact of this activity on our markets."

– Louis Morisset, CSA chair and CEO of the Autorite des Marches Financies

volatility is "not confined by borders". The two organisations have urged investors to consider the source of information and advice they are relying on to make investment decisions, highlighting that online chatrooms are "unregulated and may contact information that is inaccurate or inappropriate".

In December 2020, the CSA placed a spotlight on short selling and launched a public consultation paper in response to ongoing complaints about activist short sellers. The regulator said it wanted to explore the subject of short sellers who publicly stake out their negative position in a company with the expectation that it will negatively impact the company's share price. Issuers and other market participants complained to the regulators that it had become too easy for short sellers to publicly target companies to drive down their stock price and ultimately profit on the decline.

Louis Morisset, CSA chair and CEO of the Autorite des Marches Financies, said: "In recent years, activist short selling campaigns have received considerably more attention, and stakeholders have raised concerns about the overall impact of this activity on our markets."

In a study, the CSA found that between 2010 and September 2020, a total of 73 Canadian issuers had been the target of 116 activist short seller campaigns. The group suggested that a rise in the use of social media platforms had contributed towards the increase in activist short selling campaigns, noting that "prominent activists with a large following can promote and disseminate their short theses about target companies to a broader audience and at a much faster pace".

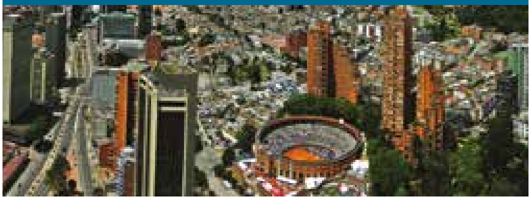
Short sellers have said they target Canadian firms because Canada is "fertile ground for corporate malfeasance" and that their research and analysis serve as an important function in the price discovery process by bringing to light new information. In most CSA jurisdictions, activist short sellers are not currently subject to any specific regulatory requirements. ■

Canada equities (US$)

	2019	2020	Q1 2020	Q1 2021
Securities lending revenues	$628,348,862	$441,605,313	$162,900,665	$74,919,361
Average loan balances	$41,069,182,111	$35,428,858,354	$35,592,583,820.66	$40,050,122,160

Source: IHS Markit

Colombia



The securities finance industry in Colombia is limited by the fact that short selling of Colombian listed securities is subject to restrictions under Colombian law.

The Colombian Stock Exchange (BVC) has continued in 2021 to try to make its markets more attractive to listing companies and investors. In May 2021, BVC and index giant MSCI launched the MSCI Colcap index, with a minimum of 25 securities and 20 issuers based on adjusted free float securities.

"This operation allows us to develop an alliance with one of the world's leading index providers and the most relevant in emerging markets such as MSCI, to manage the benchmark of our stock market, which will undoubtedly bring many benefits to the market," BVC president Juan Pablo Córdoba told Forbes.

The new index is managed by MSCI, which is solely responsible for the construction, calculation and maintenance of the index. In turn, the US company is in charge of licensing the index information to investors located outside of Colombia, as well as its use as a basis for financial products, such as ETFs and derivatives, and for redistribution purposes.

BVC handles the licensing of the index information to local investors, listing futures and options in the local derivatives market and will continue to lead information licenses in Colombia.

Speaking of the listings outlook in April, Córdoba said: "I think that 2021 will give us very good news. Today Mineros announced that it will do a dual broadcast in Colombia and Toronto. In addition, we have a registration process for a company that is also going to be a share issuer in this first semester. We also have two or three additional companies that are already in the process of joining the stock market. I believe that this year we are going to have between 3 and 5 new companies listed on the Colombian Stock Exchange in terms of equity."

Córdoba also said at the time he was unconcerned about firms delisting from the stock market, suggesting this is normal and part of the capital market process: "Everywhere there has been a reduction in issuers, it is a global process phenomenon maturation and consolidation of companies," he said. ■

Colombia equities (US$)

	2019	2020	Q1 2020	Q1 2021
Securities lending revenues	$686,312	$213,869	$32,956	$68,483
Average loan balances	$125,586,617	$94,255,287	$84,186,385	$142,124,216

Source: IHS Markit

Mexico

Mexico, one of the larger markets across Latin America, saw its equity lending revenues dip in 2020, falling from 2019's $3.2 million to $2.4 million. This drop in revenues was likely caused by the onset of the Covid-19 pandemic, which impacted equity lending revenues globally. The country's revenues picked up in the first quarter of 2021, returning $637,000 to investors, 17% more than Q1 2020's figure of $545,000, but still down from Q1 2019's $1 million, data from IHS Markit reveals.

The value of equity securities on-loan in the country, however, has increased significantly, up 27% year-on-year in the first quarter of 2021, and the highest level of growth in balances across the region. In the first quarter, average on-loan balances in Mexico were $696 million, compared to $546 million in the same period last year. Balances did increase in Mexico as the year went on, with the average sitting at $568 million at the end of 2020. However, this figure was still significantly lower than the 2019 average of $768 million.

Mexico is the second-largest economy in Latin America, second to Brazil, and its main stock exchange, Bolsa Mexicana de Valores (BMV), is the fifth largest in the region. The exchange was founded in 1933 and is now part of the BMV Group, joining Mexico's central securities depository, Indeval, the derivatives exchange MexDer, and market data provider ValMer.

In its most recent economic snapshot, published in May, the OECD reported that the Mexican economy is expected to grow

“We have been growing our presence in Mexico significantly over the past few years and are delighted to be able to offer local clients new products and solutions. With this new milestone, we are now able to offer our institutional clients a more complete pan-Americas fund services solution.”

– Francisco Hernandez, country head for Mexico at BNP Paribas

by 5% in 2021 and 3.2% in 2022. It said manufacturing exports will support growth benefiting from the strong recovery and policy support in the United States. Private consumption will strengthen gradually, aided by remittances and the rollout of vaccines. Inflation increased in the first half of the year, due to a low-base effect and higher energy prices, but it is expected to edge down.

The securities services arm of global custody bank BNP Paribas announced that it had begun operations in Mexico last year, offering the local market daily accounting and valuation services, tax pricing and regulatory reporting. Mexico became the seventh market that BNP Paribas services in the region.

Francisco Hernandez, country head for Mexico at BNP Paribas, said at the time: “We have been growing our presence in Mexico significantly over the past few years and are delighted to be able to offer local clients new products and solutions. With this new milestone, we are now able to offer our institutional clients a more complete pan-Americas fund services solution.”

Mexico’s central bank, Banco de Mexico, is one of the nine banks still taking advantage of the US Federal Reserve’s temporary US dollar liquidity swap lines. The offering, which was recently extended until December 31, was first introduced in March to support the global dollar funding markets during the Covid-19 pandemic.

The programme has been extended three times in total, once in July 2020, again in December 2020, and in June 2021. The US central bank said: “A further extension of the temporary swap lines will help sustain improvements in global US dollar funding markets by serving as an important liquidity backstop.” ■

Mexico equities (US$)

	2019	2020	Q1 2020	Q1 2021
Securities lending revenues	$3,225,251	$2,405,519	$545,086	$637,969
Average loan balances	$768,154,816	$567,658,718	$546,413,478	$696,066,640

Source: IHS Markit

United States

The US is the world's largest equity market and accounted for a significant portion of the Americas region's total revenue in early 2021. In the first quarter of this year, the US generated around $919 million in equity lending revenue. This figure represents a 28% increase compared to Q1 2020's $718 million. The market appears to have recovered well from the onset of the Covid-19 pandemic and, if the level of growth that occurred in the first quarter of the year continues, the market should out-perform 2020, which saw $3.3 billion of revenue generated.

In terms of balances, again, the figure is up significantly when compared to the same period last year, with there being more than $519 billion of US equities on-loan in early 2021, compared to $435 billion in early 2020. The balance at the end of 2020 was $428 billion.

The US equity market had a rocky start to the year after retail investors decided to take an active stance against Wall Street and bet against them. Millions of individuals piled into certain stocks, such as game retailer GameStop and cinema chain AMC, in response to hedge funds disclosing their short positions in the companies. The moves were orchestrated through social media platforms, including Twitter and Reddit, with one forum in particular booming in popularity, a SubReddit dubbed WallStreetBets, and caused a significant amount of volatility in the market.

The move sent ripples across global equity markets as regulators warned investors about the dangers of engaging in social media chatrooms that sought to drive up prices of specific stocks. The move also resulted in the US Securities and Exchange Commission (SEC) cracking down on social media touting, as it issued trading suspensions in certain stocks amid questions surrounding online promotion of certain company's securities and

"We have been working collaboratively with a wide cross section of the industry to build support for further shortening the current settlement cycle over the past year, and we have outlined a plan to increase these efforts to forge consensus on setting a firm date and approach to achieve T+1."

– Murray Pozmanter, head, clearing agency services and global business operations, DTCC

recent trading activity. The affair prompted action from the House Financial Services Committee, with Congresswoman Maxine Waters claiming that the events that unfolded "illuminated potential conflicts of interest and the predatory ways that certain funds operate, and demonstrated the enormous potential power of social media in our markets".

Following the events that unfolded in the market, a number of players called for a reduced settlement cycle for US equities, including Robinhood, an online broker-dealer that was criticised in January for halting the buying of GameStop shares.

In February, The Depository Trust & Clearing Corporation (DTCC) released a two-year roadmap for shortening the settlement cycle for US equities to one business day after the trade is executed (T+1). In order to move to a T+1 settlement cycle, market participants and regulators must align and agree to it by implementing the necessary operational and business changes. According to the DTCC, the immediate benefits of moving to T+1 cycle include a reduction in costs, reduced market risk and lower margin requirements.

Murray Pozmanter, head of clearing agency services and global business operations at DTCC, said at the time: "The time to settlement equals counterparty risk, which can become elevated during market shocks. It can also lead to the need for higher margin requirements, which are critical to protecting the financial system and investors against a firm default. We have been working collaboratively with a wide cross section of the industry to build support for further shortening the current settlement cycle over the past year, and we have outlined a plan to increase these efforts to forge consensus on setting a firm date and approach to achieve T+1."

While DTCC does not have the regulatory or legal authority to unilaterally change the settlement cycle, it has taken on the responsibility of driving this initiative forward, similar to the role it played in 2017 to move to T+2. Early indications suggested that market participants support the move to a shorter settlement cycle to take advantage of capital and operational efficiencies. DTCC estimated that the move to a T+1 framework could bring a 41% reduction in the volatility component of the National Securities Clearing Corporation's margin. The move would save the market around $250 million per day and, during periods of extreme volatility, upwards of $7 billion per day, according to Pozmanter.

The move to T+1 has been backed by two top US trade bodies, the Securities Industry and Financial Markets Association, which

represents the US securities industry, and the Investment Company Institute, which oversees US funds. Robinhood also supported the move to a shorter cycle, with its CEO and co-founder Vlad Tenev claiming that the current T+2 cycle exposes the industry to "unnecessary risk". He said: "The existing two-day period to settle trades exposes investors and the industry to unnecessary risk."

In April, the SEC welcomed Gary Gensler as its new chair. In May, the regulator revealed it is considering new rules to force firms to disclose more information about their short selling activities in what could be a significant development for the world's largest securities finance market. Gensler instructed staff to propose new guidelines around transparency in the stock loan market in response to the GameStop affair.

In April, the SEC welcomed Gary Gensler as its new chair. Gensler has previously served as chairman of the US Commodity Futures Trading Commission, leading the Obama Administration's reform of the $400 trillion swaps market. In May, the regulator revealed it is considering new rules to force firms to disclose more information about their short selling activities in what could be a significant development for the world's largest securities finance market. Gensler instructed staff to propose new guidelines around transparency in the stock loan market in response to the GameStop affair. ■

United States equities (US$)

	2019	2020	Q1 2020	Q1 2021
Securities lending revenues	$2,931,845,503	$3,348,679,470	$719,751,495	$918,716,828
Average loan balances	$457,611,267,187	$428,223,789,761	$434,912,896,146	$519,086,681,474

Source: IHS Markit

Available Now
In print or online

Log on at **directory.globalinvestormagazine.com**
to use the database of industry contacts on the move.

Supported by: HSBC Royal Bank of Canada RBC GLOBAL INVESTOR GROUP FOW ISF

ISF EQUITY LENDING SURVEY 2020
WINNER
Group 2 Borrower
Group 2 Best Relationship Manager
Natixis
PART OF GLOBAL INVESTOR GROUP

Voted most innovative Global Equity Borrower*, Natixis offers high quality solutions thanks to its in-depth knowledge of the Securities Financing market.

Collaboration || Financing || Solutions

*Group 2 - Global Market Lenders and Borrowers were split into 2 groups based on the volume traded

FINANCIAL SOLUTIONS
THAT GO BEYOND

Contact: Simon Sourigon, Head of GSF Americas & Global Head of GSF Securities Optimization
Tel: +1 212 891 1805 - simon.sourigon@natixis.com

www.cib.natixis.com

GROUPE BPCE

NATIXIS
BEYOND BANKING