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Staying consistent to core principles

Chris Jaynes outlines the main ingredients that have powered eSecLending's approach to agency lending and how the company has advanced over its 23 years in the business




SEC proposes rule changes for US clearing houses

The US Securities and Exchange Commission (SEC) has proposed rule amendments that aim to strengthen resilience, recovery and wind-down procedures for clearing agencies.

These changes target obvious gaps in current risk management and recovery procedures at covered clearing agencies.

A covered clearing agency, in SEC lexicon, is a registered clearing agency that provides the services of a central counterparty or a central securities depository.

Most significantly, the proposal requires that clearing houses have a risk-based margin framework in place that monitors intraday exposure on an ongoing basis, along with the authority and operational capacity to make intraday margin calls "as frequently as circumstances warrant".

This will include when the thresholds specified by the clearing house are breached or when products and markets display elevated volatility. These requirements appear to be fundamental to a clearing agency's effective functioning.

Second, the proposal requires that a clearing house has alternative options in place when essential inputs to its risk-based margin system are unavailable or not reliable. Again, access to required data and inputs is fundamental to a clearing agency's ability to monitor and mitigate credit risk and it is essential that access to key inputs is maintained at all times, with fall-back options in place in case of disruption, denial of service or inaccuracies in these key data inputs.

Additionally, the SEC proposal provides guidance on the content of recovery procedures and orderly wind-downs for US-based clearing houses. Prior to this, the Covered Clearing Agency Standards have required that a covered clearing agency includes a plan for recovery and orderly wind-down in its policies and procedures, but it has not specified which provisions should be included in those plans.

In the proposal, the SEC has highlighted nine elements that the clearing agency will be required to include in its plan. Inter alia, these include details of the clearing agency's payments, clearing and settlement services and how it would continue to provide these services in the event of recovery or orderly wind-down. **Continued on page 6**

Clearstream's GSF volume outstanding rises 3% YoY for April

Clearstream's Global Securities Financing (GSF) volume outstanding increased 3 per cent year-over-year to €609.8 billion for April, according to its monthly figures.

Year-to-date, its GSF business has also grown 3 per cent to €591.9 billion in volume outstanding.

Total assets under custody held in Clearstream increased by 3 per cent YoY to €17,280 billion for April, with its year-to-date AUC up 3 per cent to €17,178 billion.

In contrast, Clearstream's Investment Funds Services (IFS) business contracted over the period, with securities deposits down 4 per cent YoY for April to €3,204 billion and the number of transactions processed dropping 10 per cent YoY for April to €3.3 million.

SEC proposes rule changes for US clearing houses

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The plan will also address the clearing agency's use of third-party service providers to meet its critical payments, clearing and settlement services in the case of recovery or wind-down.

These plans should be reviewed by the clearing house's board of directors at least every 12 months or as a result of material changes to the environment in which the clearing agency operates.

Commenting on the proposals, SEC chair Gary Gensler says: 'Today's proposals would help ensure the continuity of clearing services during times of significant stress. Well regulated and well managed clearing houses help lower risk for the public.

"I am pleased to support the proposal because, if adopted, it would help to enhance the resiliency of this part of our market plumbing, which is fundamental for the capital markets to operate. That benefits investors, issuers and the markets alike."

In 2016, the SEC adopted the Covered Clearing Agency Standards, which require covered clearing agencies to implement, maintain, and enforce written policies designed to meet minimum standards relating to, among other things, operations, governance and risk management.

The recommended proposal would build upon the existing requirement in Rule 17Ad-22 that a covered clearing agency has policies and procedures reasonably designed to cover its credit exposures to its participants by establishing a risk-based margin system that, among other things, includes the authority and operational capacity to make intraday margin calls in defined circumstances.

The SEC has circulated the proposals for public consultation, which will continue for 60 days from its publication on the SEC website or for 30 days from its release in the Federal Register, whichever is longer.

Euroclear and BondCliQ launch fixed income settlement data product

Euroclear has partnered with data-as-a-service company BondCliQ to offer a new fixed income settlement data solution.

The tool provides access to refined fixed income settlement data via customised dashboards, intending to facilitate more precise portfolio management and allow users to make more informed and confident decisions.

The launch follows recent volatility in growing fixed income markets, with market participants requiring data sets that help them to monitor market performance, liquidity conditions and key trends.

Chris White, CEO of BondCliQ, says: “This is a transformative moment for fixed income markets. Until now, there has been a technology barrier to efficiently accessing and ultimately leveraging these data sets. With the BondCliQ infrastructure and technology solutions, the potential of Euroclear’s fixed income settlement data can be realised for trading, risk management, trend analysis and AI. Early adopters of this information will have a material competitive advantage.”

Phillipe Laurensy, head of group strategy for product management and innovation at Euroclear Group, comments: “As part of our data strategy we see a growing need for better insights and more in depth analysis in the fixed income settlement space. The combination of BondCliQ’s credit market data solution with the breadth and scale of a financial market infrastructure will help improve liquidity and market execution.”

Bloomberg, MarketAxess and Tradeweb sign consolidated tape joint venture agreement

Bloomberg, MarketAxess and Tradeweb have banded together to establish an independent company, JV Company, through a joint venture agreement.

The joint venture will see the firms participate in the public procurement procedure to become a fixed income consolidated tape provider (CTP) in the European Union.

The initiative reflects the desire of all three parties to improve the fixed income ecosystem and make a “meaningful” investment in winning the tender for the European bond consolidated tape (CT).

Regulatory specialist at FINBOURNE Technology and industry veteran Neil Ryan will lead the CTP initiative. Ryan has more

than 30 years of experience in various senior positions across public and private sectors, with expertise in the fixed income space.

He will focus on producing a prototype that incorporates the expertise of the joint venture parties in fixed income markets and trade reporting, to be able to deliver a high-quality CT that will provide enhanced transparency and access to robust, reliable data.

Cloud-native financial data management firm FINBOURNE Technology has been selected by the parties as the technology infrastructure provider to build and operate the CT for the JV Company — following a detailed and rigorous evaluation process, which considered critical compliance, operational, technical and security aspects of a fit-for-purpose CT.

FINBOURNE will now work closely with the joint initiative to demonstrate the capabilities and features of its proposed CT platform.

Commenting on the announcement, Ryan says: “The time has come to provide the European fixed income markets with a consolidated tape that is led by an initiative with deep experience in low-latency data processing, cleansing, consolidation and publishing within a regulated framework.

“Our motivation is to improve transparency and spur electronification in the fixed income space. Our end goal is a cost-effective CT that treats both data contributors and consumers fairly, while enabling open and impartial access to meaningful and helpful data using existing infrastructure.”

CEO and co-founder of FINBOURNE Technology Thomas McHugh adds: “We are pleased to have won the tender to work with these firms, which are deeply focused on quality data and are highly experienced in fixed income markets and running regulated Approved Publication Arrangements (APAs).

“Importantly, we see this as further validation of our modern, cloud-based, API-first technology, to deliver critical market data access and transparency.”

BrokerTec and LCH RepoClear expand partnership

Electronic trading platform and technology firm BrokerTec has expanded its partnership with LCH RepoClear.

Users of BrokerTec Quote, the company’s

dealer-to-client request for quote repo trading solution, will now be able to clear euro-denominated securities on the platform with LCH RepoClear.

RepoClear's sponsored clearing feature allows buy-side market participants to clear their transactions with the dealer of their choice via the sponsorship of an agent, facilitating euro-denominated repo trading with the benefits of a central counterparty. This enhances existing clearing relationships, the company says.

Commenting on the announcement, John Edwards, global head of BrokerTec, says: "This improved functionality for existing and new clients will help further accelerate trading opportunities on BrokerTec Quote, our rapidly growing bilateral, relationship-driven alternative execution service to our market leading central limit order book for repo transactions."

Emmanuel Rolland, chief operating officer of RepoClear, collateral and liquidity management at LCH, adds: "With this collaboration, the buy side is able to gain greater access to LCH RepoClear, the largest liquidity pool for cleared Euro-denominated government bonds, while banks can benefit from netting opportunities thus alleviating their resource management pressures."

S&P Global Market Intelligence updates performance measurement tools

S&P Global Market Intelligence has built a new capability that allows data contributors to report their off-line revenue adjustments, which will be included in the firm's performance measurement tools.

The move highlights the firm's adherence to the International Securities Lending Association's (ISLA's) best practice guidelines for Securities Lending Performance Management (SLPM).

According to the firm, these adjustments can be added at entity and security level for a specific date or month (lump sum amount) and for up to five years of historical adjustments.

This aims to further improve the performance analysis of a securities lending programme.

Commenting on the announcement, Kabin George, global head of product management, securities finance at S&P Global Market Intelligence, says: "The inclusion of these adjustments would result in a more accurate representation of how lending programmes are performing against their peer groups.

"The adjustments to the revenue are processed and reflected instantaneously in the performance analysis tools of our securities finance products."

Archegos and gilts crisis motivates tighter FCA scrutiny

The Financial Conduct Authority has called for better data coverage to monitor risk concentrations in the non-bank financial intermediary sector.

In a recent presentation to the Managed Funds Association Global Summit, FCA chair Ashley Alder notes that prompt action is necessary to enhance reporting from non-bank financial intermediaries (NBFIs) and to establish better frameworks for monitoring levels of leverage, including hidden and synthetic, in this sector.

The FCA believes that NBFI entities need to disclose their exposures more fully to prime brokers, banks and other firms that provide finance or serve as derivatives counterparties, thereby enabling these intermediaries to evaluate levels of leverage and concentration risks more effectively across their clients.

It points to the collapse of Archegos as an example, involving a private fund receiving finance and other services from regulated prime brokers and trading using total return swaps and a range of other instruments.

It also looks to learn lessons from the UK gilts crisis, where liability-driven investment funds experienced difficulties in meeting margin calls as gilts yields spiked, triggering dysfunction in government bond markets as LDI funds made forced sales to meet collateral calls.

For the FCA, the growing importance of financial intermediation by non-bank financial intermediaries cannot be underestimated. As public and private debt has mushroomed during the recent period of central bank quantitative easing and low interest rates, NBFI has grown to account for about 50 per cent of global financial assets.

This is explained, in part, because government debt and corporate debt markets have grown too quickly for banks to deal with themselves, particularly in the face of balance sheet constraints imposed by stronger post-2008 capital adequacy requirements. With this, investment funds and private markets have stepped in to partially fill the gap.

Alternative investment fund managers are already regulated in this area to a degree, being required under the Alternative Investment Fund Manager Directive (AIFMD) to demonstrate that their leverage limits are reasonable and that they are operating within those limits.

But investment funds perform a substantially different structural function in these markets to organisations that hold bank licences. The risks are commonly distributed across end investors' balance sheets, rather than being carried by NBFI entities themselves.

NBFI entities typically act as agents or fiduciaries without assuming balance sheet risk and without offering deposit insurance or any form of indemnification to the investor.

With this, the FCA advises that there should be three main pillars to evaluating NBFI risk in private markets. This requires a solid understanding of off-balance sheet leverage. It demands a better appreciation of liquidity risk. And it calls for better information about exposure levels across traditional banks and private markets.

There is currently little data disclosure or reporting from private markets, the FCA suggests, and international cooperation across financial supervisors is required to address this shortcoming.

Among other initiatives, the Financial Stability Board (FSB) is conducting research on NBFI leverage, with a primary focus on prime brokers, hedge funds and family offices.

The FSB and IOSCO are conducting combined research on equity swaps — although the FCA's Alder points out that derivatives trade repository data provided little earning warning of risk concentrations prior to the collapse of Archegos for example.

In response, the FCA indicates that it has signed memorandum of understanding (MoUs) with European authorities that illustrate their commitment to cooperating on NBFI supervision and to sharing data and information to enable better oversight.

SmartStream and Acadia collaborate on collateral management solution

Financial transaction management solutions provider SmartStream Technologies has extended its partnership with margin automation services firm Acadia.

SmartStream's Transaction Lifecycle Management (TLM) collateral management solution will be available through Acadia's Margin Manager, alongside the latter's substitutions workflow product.

Together, the companies will offer automated two-way communication and substitution coordination between counterparties, with substitution details managed in a standardised format through the workflow lifecycle.

The partnership will improve processing and calculation efficiency of substitutions movements for TLM collateral management clients and their counterparties, the companies say, providing exceptions-based processing and promoting straight-through processing for collateral substitutions.

Jason Ang, programme manager at SmartStream's TLM Collateral Management, says: "Given the current emphasis for optimisation in the market, we see that there will be an increase in substitutions requests. These requests traditionally have been a time-consuming process, but we have worked to provide an automated solution to help our clients save time, reduce manual work, and automate the process.

"TLM Collateral Management, coupled with Acadia's Margin Manager, provides integration with a powerful collateral management solution, and a user-friendly dashboard allowing for quick exception management, with a complete audit trail with final statements."

Staying consistent to core principles

eSecLending's president Chris Jaynes speaks to Bob Currie about the main ingredients that have powered the company's approach to agency lending and how clients are pushing for greater alignment between their securities lending, financing and treasury management functions

Chris Jaynes was one of eSecLending's founders when the company was created in 2000 and the CFA charterholder has worked at the Boston-based lender since its creation, previously as chief operating officer, as co-CEO and currently as president.

Since the company was founded in 2000, eSecLending has grown to become one of the largest lending agents in the market, with more than US$100 billion in assets on loan, and it features some of the world's largest pension funds, asset managers, insurance companies and sovereign wealth funds among its client base.

Having helped to guide the company from infancy to adulthood, Jaynes is well placed to evaluate how its core principles have evolved over almost a quarter-century and the direction in which clients' lending and financing requirements are leading its strategy.

Reflecting on this evolution, Jaynes tells SFT that the focus of eSecLending's strategy since formation has been on delivering flexible market access to its clients, offering exclusives alongside discretionary lending and employing proprietary auctions as a means of price discovery for the lender prior to making their execution decision. These principles have been central to the company's approach, he explains, and a key differentiator for its business.

Overarching these delivery mechanisms has been the provision of segregated and customised lending programmes for its clients. For each lender, eSecLending provides a segregated, bespoke lending programme that is tailored explicitly to the objectives and strategy preferences of that customer.

Having grown initially out of the securities lending business of an asset management company, United Asset Management, the founders recognised the virtues of this segregated, customised approach to lending as a way to address the shortcomings of competing offers provided by the large custody banks that operate through pooled lending structures.

"As a buy-side lender, we had specific expectations in terms of flexibility and control over how our assets would be managed that we felt were best served through a segregated, individually managed programme — and this was hard to find in the market at that time," he says. As founders, they valued the flexibility offered by having a choice of routes to market, with exclusive strategies available alongside discretionary lending. "Lending within a large pooled programme did not offer what we were looking for in terms of flexibility and control, nor did it meet our expectations in terms of transparency," he adds.

It was this experience as a buy-side lender that defined the team's approach on launching eSecLending. For an agency lending desk at a large custodian bank, it is impractical to tailor an individualised, segregated lending programme for each of several hundred clients — a pooled approach thrives on offering a broadly standardised lending model and delivering efficiencies through scale.

In contrast, eSecLending identified a demand for bespoke solutions from some of the world's largest institutional lenders, enabling them to earn a substantial premium from their loan inventory and to benefit from the transparency and price discovery offered by eSecLending's proprietary auction programme, whereby borrowers submit blind bids for the client's portfolio or for a parcel of assets within that portfolio.

For Jaynes, the auction process generates premium returns for certain asset classes and markets and the pricing transparency provides the lender with the information to make better-informed execution decisions. All bids from borrowers are legally binding and when an attractive bid is received, this may provide an opportunity to increase revenues by lending through an exclusive arrangement. For assets where the bids do not offer a revenue premium to the market, the lender is often best served by lending on a discretionary basis.

Looking back over the evolution of the business, Jaynes notes that the firm's core strategy and approach to the market has remained consistent since its creation, but he focuses on two main areas that have changed over time. First, the depth and breadth of the firm's client base and service offerings have broadened significantly. In the initial years, the team was focused primarily on exclusives and equity portfolios for US-based clients, but subsequently they have extended the scope of eSecLending's services to include discretionary and exclusive lending in all asset classes and markets globally.

The client base has expanded, with the business supporting clients across Europe, the Middle East and now Asia. The team is also doing more to support their clients with solutions to manage the collateral management and financing needs of the major institutional investors that they service.

A second important change is linked to the growth of the management team. Some key managers, like Jaynes, have been with the company throughout the early years. Over time, however, the business has added senior executives from several of its large custodial and third-party competitors, creating a deep bench of talent and a management team with experience that, Jaynes believes, cannot be matched by any other firm in the market.

Alternative trading structures

In financial services, every business decision is to some degree shaped and constrained by regulation — and securities finance aligns with this general rule. For the service provider, the skill is to help the client to negotiate this rules-driven adaptation process and to take advantage of the opportunities this presents.

For eSecLending, unsurprisingly, a priority is to assist borrowers with managing the balance sheet impact of their borrowing activity and to fulfil liquidity standards imposed under liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) obligations. In the wake of the global financial crisis, financial supervisors have reinforced steps to ensure that banks have strong capital positions, complemented by liquidity standards designed to ensure the resilience of a bank's funding profile over a 30-day and one-year timeframe.

To optimise lending opportunities, the firm has implemented alternative trading structures and identified trades that best match a borrower's needs to the risk tolerance and collateral eligibility criteria applied by lenders. "Again, we believe that offering segregated account structures offers significant advantages, enabling eSecLending to engage in detailed individual discussions with clients and the flexibility to implement bespoke trades that best match the requirements of borrowers and each individual client," says Jaynes.

In recent times, the industry's focus has turned to lender indemnification and the widely-publicised pressures that this puts on lending agents in terms of the balance sheet cost of lending. The regulatory capital cost of providing loan indemnification for the agent lender is estimated to be between 10 and 14bps under the Basel III bank capital adequacy regime and this will continue to represent a significant overhead with implementation of Basel IV.

Trade bodies have highlighted a need for dialogue, with some commentators indicating that agent lenders will need to adjust their pricing, or lenders will need to forfeit their requirement for indemnification, for agent bank intermediation in securities lending trades to remain economically attractive. Participants at the Bank of England Securities Lending Committee meeting in March proposed that, given returns on securities lending are relatively low, the bulk of lending is unlikely to be profitable for the lending agent if they continue to provide indemnification to the lender. Jaynes indicates that this regulatory environment is creating additional opportunities for eSecLending, since as an independent firm that provides indemnification through insurance, it is not impacted by the increased capital costs that are putting pressure on the large custody bank programmes.

A few large beneficial owners have now waived their indemnification, notes Jaynes, but this has been the exception rather than the norm. Typically these firms have committed a lot of time and resources to enhancing their own internal trading and risk management structures such that if there was a default, they will be in a position to manage that unwind. However, the vast majority of clients are not in this position and will continue to expect their agent to provide indemnification.

In practice, it is a challenging decision for senior management of a beneficial owner to forgo that indemnification, often with little obvious upside for the firm or individuals concerned," observes Jaynes. "Consequently, we do not see agent bank indemnification disappearing from the market. In recent months, we have seen increased interest in our services from lenders who are being presented with difficult choices on indemnification from their existing agents."

Peer-to-peer engagement

As central banks tighten interest rates and signal the potential unwind of their long-running asset purchase programmes, buy-side firms continue to seek new sources of financing and look to diversify their funding counterparties.

In this context, P2P lending refers to direct lending of cash or securities from beneficial owner to beneficial owner — referring to financing or securities lending relationships between large pension funds, insurance companies, sovereign wealth funds and asset managers, for example.

Jaynes indicates that there has been a meaningful upturn in this type of direct lending between beneficial owners in recent years —

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Chris Jaynes
President
eSecLending

although this typically serves as a supplement to traditional trading activities rather than replacing them. Some large beneficial owners are seeking alternative sources of financing through direct lending channels, potentially offering better pricing and better stability of supply — for example over period ends when liquidity conditions can tighten substantially.

For counterparties, Jaynes identifies three primary barriers to the expansion of P2P lending and financing — specifically legal, credit approval, and operational support — and he indicates that eSecLending provides support for clients in each of these areas.

The first is the challenge of managing legal documentation. If a peer wishes to trade with 10 different counterparties, this commonly requires that they set up bilateral legal documents with each of these trading parties. This documentation overhead can be a significant obstacle to peer-to-peer, particularly for beneficial owners that do not have a large in-house legal department. "Sitting in the middle of these trades, we make the legal overhead substantially easier for the client," he says. "By utilising eSecLending to administer these transactions, clients can leverage the broad library of contracts that we already have in place, thereby reducing the burden of establishing bilateral documentation directly with each of their P2P counterparties."

There is also a significant operational overhead in managing P2P lending — from managing trade and settlement instructions, to moving and valuing collateral, to managing lifecycle events across the life of this securities financing trade — and many beneficial owners are not set up to manage this in house. Consequently, using a specialist agent such as eSecLending can offer significant advantages in managing this operational complexity.

A third prominent challenge is in managing counterparty risk. "eSecLending is well positioned to assist peers in evaluating the credit risk associated with their lending and financing relationships and will also provide indemnification over peer-to-peer activity," says Jaynes. "Whether a pension fund is lending assets to a bank counterparty such as a prime broker, or it is lending to another pension fund, we have indemnification insurance in place and provide confidence that clients' assets are protected across the term of the loan agreement."

In these key respects, Jaynes suggests that eSecLending is different from other peer-to-peer matching and lending platforms. Few of these solutions, he believes, have solved effectively for the credit risk component or provided an effective solution for the operational challenges. And few have developed an effective solution to manage the legal documentation.

Although some beneficial owners, particularly in the Canadian market, are now lending P2P and managing their trading requirements directly, Jaynes indicates that as peer-to-peer activity continues to grow many lenders will continue to require third-party support for the associated legal, operational and counterparty risk management obligations.

Changing business practice

More broadly, a number of factors have been important in driving changes in how securities lending business is conducted. One has been the need for borrowers to manage the capital impact of their lending activity as efficiently as possible.

A second has been a drive for lenders to align their securities lending activity more closely with their broader financing and treasury management functions. Traditionally, securities lending has operated as a distinct and separate business silo established to generate additional revenue from a lender's asset portfolio.

In recent years, many pension funds and asset managers are recognising that securities lending can be a valuable tool to support collateral transformation and to ease their financing requirements by using cash received as collateral. By utilising securities lending within their overall treasury management function, clients can lower financing costs and reduce their reliance on bank financing while at the same time reducing the risk of reinvesting cash collateral by mobilising it to meet in-house requirements.

This same message applies when borrowing securities. Buy-side firms running long-short strategies typically source their borrowed securities from the Street, when in many cases the required securities are sitting in inventory under the control of another business area within the firm. Lenders are increasingly working across business units to access internal supply and to make optimal use of liquidity and inventory at the enterprise level.

But this drive to break down silo-based approaches to trading, liquidity and collateral management has been ongoing for decades

— and many firms claim they have made major advances in reducing this fragmentation over the past 20 years. So how far has the industry advanced in this area?

“US pension plans have traditionally been heavily siloed and have tended to source their cash and securities requirements largely through banks and broker dealers,” responds Jaynes. Until recently, there has been little use of internal supply or direct financing activity between large beneficial owners. However, this is changing with pension funds, insurance companies and sovereign wealth funds making better use of internal assets and taking advantage of their balance sheet strength to lend directly to each other through P2P transactions.

This upturn in P2P lending has aligned with traditional borrower counterparties pulling back from certain types of repo or securities lending trades, typically due to the narrow spreads and the reduced economic benefit as a result of increased regulatory and capital costs. P2P lending has helped to fill this void, adding capacity and supply and delivering the risk management benefit of wider counterparty diversification.

More generally, trading strategies are becoming more creative to meet the evolving needs of both borrowers and lenders. This may be through structured trades that deliver capital-efficient lending structures to the borrower, while ensuring they meet lender-specific guidelines and risk tolerances. “By offering flexibility through our segregated account structure, this puts eSecLending in a strong position to facilitate tailored transactions that pair borrowers directly to lenders to enable trades that benefit both parties,” says Jaynes.

Concluding thoughts

In wrapping up, Jaynes notes that he has seen a significant shift in how large asset owners are approaching their lending strategies in the 23 years since eSecLending was established. Most large pension funds, insurance companies, sovereign wealth funds and asset managers are employing multiple routes to market and are utilising specialist third-party providers, direct lending, or both, for at least a part of their loan book. Any large beneficial owner that is lending wholly through their custodian bank is an outlier today, while this was the norm back in 2000.

For large client portfolios, which will benefit from lending outside of a pooled structure, he believes that a segregated and individualised approach has proven to be very effective. “As a dedicated securities financing business, we offer the additional assurance to clients that our focus is exclusively on providing securities financing and related services and we are not competing with other business units for development resources,” he comments.

Looking historically, collateral eligibility criteria have certainly widened over the past 15 years. Prior to the 2008 financial crisis, a large majority of US clients favoured cash collateral, while most European clients were predominantly accepting non-cash. With the crisis, many US collateral takers have moved to a balance of cash and high-quality non-cash collateral. On the borrower side, banks are now looking to borrow against a range of non-cash collateral that extends well beyond US treasuries.

“With changes to guidelines in recent years most large pension funds today will accept cash, sovereign debt, main index equities and certain ETFs as collateral,” says Jaynes.

More broadly, Jaynes notes that many beneficial owners are expanding how they employ their securities lending strategies, not simply to generate intrinsic income but as an integral component of their financing strategies.

Projecting forwards, Jaynes predicts that asset owners will continue to move towards centralised treasury, breaking down silos and integrating securities lending more closely with their overall financing and treasury activities. He also expects to see further growth of peer-to-peer financing in coming years, with eSecLending continuing to play a key role in that expansion.

Geographically, eSecLending will continue to grow in North America and Europe and it expects further expansion in the Middle East and Asia Pacific, where their business pipeline is strong. “Though we have an active client base across these locations currently, we anticipate the percentage of our global footprint in the Middle East and Asia Pacific will grow as we continue to build upon opportunities with our bank partner, Standard Chartered,” says Jaynes. He notes that eSecLending is active in all asset classes and markets that can support securities lending from a regulatory and fiscal standpoint around the world. “In this capacity, the future is bright for our growth strategy across our North America, EMEA and APAC activities,” he concludes.

Securing the repo lifeline: how technology is driving the market

Demand for automation, workflow and straight-through processing is on the rise in an expanding repo market. Industry participants discuss the pain points for new entrants and the complexities within this space as they drive for further standardisation. Carmella Haswell reports

Repo trading — a lifeline to capital markets for primary issuance and secondary market liquidity, and an important investment and funding vehicle for the broader securities finance industry — continues to grow.

One consequence is that banks and asset managers are increasing investment in their post-trade capabilities to support the expansion of their repo market activities, notes HQLA^{X} CEO Guido Stroemer.

"If you look at collateral management and repo, it used to be viewed as an operational headwind that institutions supported with limited strategic planning," Stroemer confirms. "But now, it is transforming into a strategic differentiator. Firms that manage collateral efficiently can differentiate themselves and deliver meaningful bottom line results for their shareholders."

A recent European Repo Survey revealed that the total value outstanding of repos and reverse repos on the books of 61 institutions on 8 December 2022 had grown to a record high of €10,374.2 billion, a 12.8 per cent rise year-on-year. Furthermore, data provided by automatic trading systems (ATS) in Europe pinpointed a further acceleration in the growth of repo trading value.

According to the International Capital Market Association (ICMA) European Repo and Collateral Council (ERCC) survey, the outstanding value of repos executed on these platforms increased 15.7 per cent to €1,651.4 billion on 8 December 2022, compared with the previous survey in June 2022.

With rapid growth in the market, industry participants are reviewing the evolving repo space and how technological innovation can be leveraged to support its enhancement.

For Ed Tyndale-Biscoe, product owner for secured funding at ION Group, there has been a "sea change" in the way people view technology and what it is capable of — due, potentially, to the pandemic and the wider need for people to be able to communicate more effectively. Repo, according to Tyndale-Biscoe, has "historically been something of a back office, less of a front-office focus, profit centre-minded business". He notes that the technology in the repo space has been "undeserving of the business".

"The hybrid nature of the market is changing. The interdealer markets, which are a fundamental part of how wholesale operations work, the RFQ platforms, which allow other participants to access those markets, the integration complexity to deliver all the necessary decision-making inputs and the cognitive load this implies from the front office point of view have created a complex situation," says Tyndale-Biscoe.

Managing this setup on a desktop — with several different screens, inventory, pricing, real-time or T+1 margin — is "impossible", notes Tyndale-Biscoe, unless it is fully integrated and totally standardised, front-to-back.

Addressing the addressable market

Technology is driving a market solution, technology is not leading us to a market solution, says Travis Keltner, global head of repo financing at State Street.

Keltner notes that to identify a solution, it is imperative to adapt to that market and understand the problems and challenges it presents, as well as the opportunities to leverage technology. “As related to repo, it is key to understand the foundational makeup of our current short end as it has changed dramatically over the last few years,” he adds.

Regarding the overarching macro landscape at the short end, Keltner makes reference to the recent headlines highlighting concerns around the “debt ceiling”, suggesting that there are going to be “all types of questions evolving” and a “number of money market considerations” around this.

Also known as the ‘debt limit’, the debt ceiling is the maximum amount of money the US Congress allows the federal government to borrow to cover its bills. As the government edges closer to its debt limit, Congress has yet to decide whether to raise or to suspend the ceiling. Headlines have reported fears that if the ceiling is not raised, then this could cause the US to default on its debt and, potentially, lead to major economic damage.

Once dominated by email, excel sheet and telephone calls, the repo market is now facing a demand for automation, workflow and straight-through processing (STP) from a post-trade perspective. Colleen Stapleton, product manager for match and repo products at MarketAxess, says the catalyst for this shift came from the introduction of the Central Securities Depositories Regulation (CSDR) and the conversations around the looming T+1 settlement cycle — which will come into effect in May 2024 for the US and Canada.

Stapleton indicates that middle-office and operations personnel now understand the need to insert technology, automation and efficiency into their workflows. Although the industry does not appear to be there yet, in terms of standardisation in the repo market, Stapleton is confident that “we are getting there” with the help of industry working groups.

However, at MarketAxess, the firm is finding pain points with booking behaviours around events. Stapleton indicates that certain counterparties have bought into an event workflow, while other counterparties are very focused on a cancel repo workflow. “When you are looking for STP opportunities and bringing communities together,” Stapleton observes, “those kinds of differences lead to bottlenecks.”

Stapleton calls for action in this respect, where the industry, as a community focused on securities finance, looks for additional security and standardisation opportunities, especially around booking, rerates and new prices. “All of this leads to the bottomline, which is the need to continuously build our operational resiliency through STP platforms with solution providers, to help reduce some of the touch that our operational professionals are dealing with today,” she adds.

Time is of the essence for any reporting cycle or settlement cycle, affirms Mark Pekala, vice president of fixed income product management at Broadridge. He continues: “In that regard, it is of the utmost importance to have higher STP rates so that we can bridge the gap between the front, middle and back-office ecosystem, so that they are interoperable, so that everything is in sync with one another.”

For Pekala, interoperability has to be key so that every platform is compatible, he says, so that any solution offered is compatible with another solution. “This way, it really drives the innovative spirit of STP across the board and eliminates bottlenecks, which are of the utmost urgency and importance.”

“The addressable market for repo is underestimated,” says Keltner. Executing repo for market participants is not a simple process, it is not just a trade but also matching, systems integration, settlement and delivery, not to mention margining and reporting. Keltner describes the technology in this space today as “really powerful”, as the entity can be used to expand the addressable market and bring in additional repo participants. However, connecting the right technology vendor and partner with the right user is “not an easy dance”.

While industry participants look to expand the repo market, new entrants are facing barriers to entry from a technology point of view. Tyndale-Biscoe explains that this is due to the difference between the systems involved as well as the complexity of the integration landscape. Furthermore, the budgets required to deploy a complex solution are significant, although these are gradually decreasing, according to Tyndale-Biscoe.

Tyndale-Biscoe indicates that as technology becomes more standardised in the repo segment, vendors will be able to deliver much more “shrink-wrapped” or “out-of-the-box” solutions, which are easier to manage and more cost effective from both the end user and vendor perspective. He concludes: “That is an important aspect of how to grow the size of the market globally and increase the addressable market.”

Government debt powers growth in 2023 lending revenues

During 2022, US$1.8 billion in revenues were generated from government bond lending, making it one of the best years to date for the asset class. Matthew Chessum, director of securities finance at S&P Global Market Intelligence, explains the factors driving this vibrant demand for sovereign debt

Government bond markets have encountered one of the most active and unpredictable environments experienced for many years. Since the global financial crisis, a prolonged period of central bank support, abundant liquidity and low interest rates has suppressed both yields and spreads across this asset class. The emergence of global economies from the grips of the Covid pandemic and the subsequent inflationary pressures have acted as the stimulus for a change in monetary policy and a return to a more normalised interest rate environment.

Over the past 18 months, government bonds in the securities lending markets have been benefiting from this change in market conditions. During 2022, an incredible US$1.8 billion in securities finance revenues were generated by the asset class, making it one of the best years to date for government bond lending. Since January, over US$646 million in revenues have been generated for lenders, which is an increase of 12 per cent over the same period during 2022. With revenues 13 per cent higher during Q1 2023 than in the equivalent period of 2022, the asset class is experiencing a very strong start to the year. Looking at securities finance activity for 2023, government bonds appear to be improving upon the strong performance experienced during 2022 across all geographical regions.

Europe

Average fees for European government bonds hit a monthly average high of 21bps for the first time during November 2022. This fee was maintained through to February 2023 before declining month-on-month to 18bps during April 2023. Revenues reflected these higher fee rates, with an average increase YoY of just over 12 per cent for the January to April period. Over a similar period, utilisation hit highs not seen for many years, peaking at 30.8 per cent during October 2022.

Across Europe, UK (at US$62.9 million), French (at US$48.4 million) and German (US$71.9 million) government bonds continue to generate the highest revenues for lenders. Utilisation in UK gilts remains above 30 per cent, after reaching an all time high of 38.9 per cent during September 2022. Average fees for UK gilts reached 32bps during November 2022 and currently equal the European government bond average of 19bps.

During 2022, Italian government bonds increased in popularity among borrowers. Utilisation averaged 24.29 per cent over 2022 (compared with 19.26 per cent in 2021, and 14.16 per cent in 2020) but peaked at 30.65 per cent during the month of November. Average fees also stood at a multi-year high during April 2023 of 14bps, after averaging 10 bps during 2022, 7bps in 2021 and 8bps in 2020.

Greek government bonds have also been making a comeback over the past year. This may be the result of market participants taking a view following the recent elections or end investors expecting some reversion now that the country's 10-year yield is lower than Italy's. This may also be down to borrowers becoming more comfortable with accepting the country's debt as collateral, following years of fiscal tightening and the possibility that the country could become investment grade by the end of the year.

Balances in Greek government bonds increased 38 per cent during April to just under US$200 million. As balances have increased, average fees have been declining but still stand at a very respectable 74bps (with a 100bps average for Q1 and a 2022 average of 115bps). Utilisation of Greek government bonds has been increasing month-on-month during 2023 and currently stands at 6.08 per cent. Q1 average balances were 93 per cent higher YoY — relative to 4.55 per cent for 2022, 3.48 per cent for 2021 and 1.74 per cent for 2020).

Americas

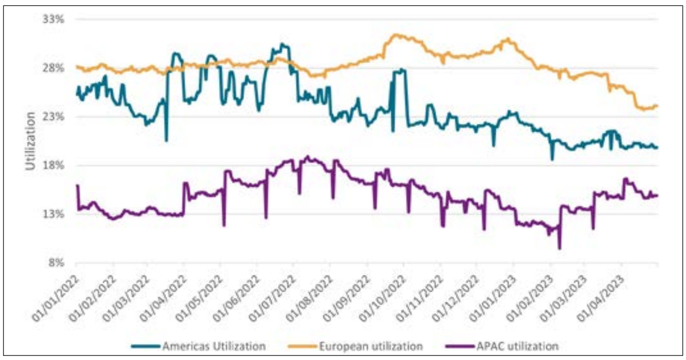
Across the Americas, government bond markets continue to be dominated by the US$24 trillion US treasury market. Discussions regarding the US debt ceiling have recently been increasing volatility in volume-weighted average fees as investors continue to pay close attention to ongoing discussions regarding the debt ceiling (Fig 1).

Fig 1: Volume-weighted average fee (VWaF) for government bonds by region

Lending in US treasuries generated US$941 million in revenue during 2022, which is another all-time recent high — situated against recent revenues of US$898.3 million in 2021 and US$865.2 million in 2020. During Q1 2023, revenues increased 9.1 per cent YoY to US$238 million — with US$319.6 million being generated year-to-date.

Average fees are reflective of this increase in revenues. Average fees hit 20bps during December 2022 for the first time since April 2020, when strong demand generated by the onset of the Coronavirus pandemic increased the average fee. Utilisation has been decreasing across US treasuries after hitting a monthly average high of 28.05 per cent during 2022 (Fig 2). Utilisation fell below 20 per cent to 19.61 per cent in April 2023 for the first time since February 2020.

Fig 2: Government bond utilisation by region



A similar pattern has been emerging across Canada. Utilisation fell to 18.81 per cent during April, marking a multi-year low. However, average fees maintained a healthy 15bps throughout 2023, which is again a multi-year high. Balances over the Q1 period were 16 per cent lower YoY. Year-to-date revenues have risen to US$50.8 million, relative to US$47 million during the same period in 2022.

Asia Pacific

Across the Asia Pacific region, the market remains dominated by a handful of countries. Average lending fees for government bonds have been in decline across the region, after hitting an impressive 27bps in January this year. The elevated average fees have translated into stronger revenues for lenders. US$96.7 million was raised during 2022, which was significantly higher than the US$56.2 million generated in 2021 and US$34.1 million in 2020. Revenues during 2023 have so far extended this trend, illustrated by an average increase of 44 per cent month-on-month.

A lack of liquidity in Japanese government bonds — caused by the ongoing yield range regulation used by the central bank of Japan to control bond prices — continues to push average fees higher, hitting an all-time high of 32bps during January. Fees have subsequently declined month-on-month to 25bps during April. Revenues produced by JGBs continue to outperform, generating annual revenues of US$54.5 million during 2022 — which compares favourably with the US$46.4 million raised in 2021 and US$22.8 million in 2020.

Australia is also a supplier of high-quality liquid assets within the region. Average fees have increased significantly over the past year, starting 2022 at 9bps and hitting 22bps during January 2023. Utilisation has been declining, however, after reaching an all time high of 32.23 per cent during July 2022.

South Korean government bonds have started to become more popular with borrowers. The country has a strong credit rating and its bonds are increasingly recognised as high-quality liquid assets. Utilisation surpassed 5 per cent for the first-time during September 2022 and average fees have remained over 20bps during the entirety of 2023.

As we have seen, government bonds continue to perform well, despite the many challenges that the market has been facing. Revenues remain robust across all markets owing to elevated average fees. The specials market continues to thrive across jurisdictions, owing to the hawkish interest rate environment. Based on current market trends, government bonds are likely to remain one of the best performing asset classes of 2023 and may even surpass the remarkable returns generated during 2022.

Major moves in leadership at State Street, Goldman Sachs and Kayenta

State Street has appointed Patricia Hostin as global head of its Agency Securities Lending business.

Based at the firm's Boston headquarters, Hostin will be responsible for overseeing the entire business globally, while working collaboratively across key business and support functions to ensure State Street delivers its securities lending product.

Hostin will report directly to Gino Timperio, global head of financing solutions for State Street Global Markets.

Bringing more than 20 years of experience to the firm, Hostin was most recently managing director for BlackRock's Financial Resource Management business.

In her former role, Hostin executed BlackRock's global strategy for optimising capital and balance sheet consumption, with broker-dealer counterparties across repo financing, securities lending, prime brokerage financing, cash management and trading.

Hostin was also a member of BlackRock's Balance Sheet Steering Committee, BlackRock's New York Leadership Team and is a Risk Management Association (RMA) Committee representative.

The announcement marks another key appointment for State Street, following on from the hire of Taryn Siglain, who was selected as the firm's new global head of Enhanced Custody — State Street's principal securities lending programme.

State Street says that Agency Securities Lending has been a core business unit within the firm for more than 50 years, with nearly US$5 trillion in lendable assets and an 'extensive' global operating model.

Commenting on the senior appointment, Timperio says: "We are very excited to welcome Patricia to State Street, as she's a seasoned leader who joins us at an optimal time to provide important leadership to our agency securities team.

"Her experience in the industry, coupled with her strong leadership background, will prove invaluable as we look to further strengthen our lending business to meet the multifaceted needs of our clients."

Citi appoints Shepherd

Citi has appointed Chloe Shepherd as assistant vice president and credit repo trader.

Shepherd joins Citi's London office from a five-year tenure at RBC Capital Markets, where she was most recently associate repo trader. Prior to this, she was a credit trading analyst at the firm.

Shepherd was previously a summer analyst at RBC Capital Markets within the firm's global markets sales and trading division in 2017.

Earlier in her career, Shepherd was an ambassador for Female x Finance from 2021 to 2023, an organisation which aims to increase female presence in the financial sector.

As the Securities Finance Times Industry Excellence Awards draws closer, Shepherd has been shortlisted for this year's Rising Star category. The awards are to be held at Plaisterers' Hall, London on 6 July 2023.

Hostin adds: "I am pleased to join State Street and I am looking forward to working with a talented team of agency lending professionals to deliver for our clients."

Nehal Udeshi has departed from her position at Goldman Sachs after 17 years with the firm.

Most recently known as global co-head of cross-asset financing and co-head of equities funding and financing structuring at Goldman Sachs, Udeshi worked within the firm's New York office.

Udeshi took on a number of senior positions during the 17-year period with the company, including head of Americas cross-asset financing and equities structuring funding.

She first began her tenure at Goldman Sachs in London within the firm's foreign exchange trading business.

Kayenta, a hedge fund software solutions developer with a focus on treasury functions, has appointed Reinhardt Olsen as chairman of its board of advisors.

Olsen brings more than 30 years' experience within the financial services sector. He was most recently head of global family office and unified one client, Americas at UBS.

During his 19-year tenure at UBS' New York office, Olsen held a number of senior positions including managing director, head of equities Americas and managing director, global head of prime brokerage.

Previously, Olsen spent almost 14 years at Merrill Lynch (now Merrill) where he was a managing director with senior responsibilities across capital markets, sales and trading.

The board of advisors offers counsel to help Kayenta in developing a treasury management system. The firm first launched in March 2021 to target allocation inefficiencies between hedge funds and prime brokers by offering a cloud-based, modular platform that promises to reduce the high costs of financing.

In an online statement, a Kayenta representative said: "Following a successful career in senior management at UBS, Olsen brings a wealth of personal expertise and we are privileged to have him chair the group.

"We look forward to collaborating closely with Olsen and the rest of the board as we work towards achieving our shared vision for Kayenta."

Northern Trust has appointed Joe Jackson within its EMEA securities finance trading team.

Based in London, Jackson will work on the agency lending desk as a securities finance trader, where he will cover the trading of fixed income and equity securities.

In his role, he will report to Joseph Gillingwater, global head of fixed income securities finance trading.

Jackson joins Northern Trust from BNY Mellon, where he most recently worked within the bank's securities lending middle office.

Previously, Jackson was a consultant at Vantage Point and, before that, a credit bond middle office analyst at Nomura.

Publisher: Justin Lawson
justinlawson@securitiesfinancetimes.com
+44 (0) 208 075 0929

Group editor: Bob Currie
bobcurrie@securitiesfinancetimes.com
+44 (0) 208 075 0928

Deputy editor: Jenna Lomax
jennalomax@blackknightmedialtd.com
+44 (0) 208 075 0925

Senior reporter: Carmella Haswell
carmellahaswell@securitiesfinancetimes.com
+44 (0) 208 075 0927

Reporter: Lucy Carter
lucycarter@blackknightmedialtd.com
+44 (0) 208 075 0925

Accounts: Chelsea Bowles
accounts@securitiesfinancetimes.com
+44 (0) 208 075 0930

Designer: James Hickman
jameshickman@blackknightmedialtd.com

Marketing director: Steven Lafferty
design@securitiesfinancetimes.com

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