Securities Finance / Securities
Based Lending (SBL)

01 What are the major securities lending platforms (Equilend, Pirum, etc.) doing to help the industry get ready for T+1? Are they not the main enablers for us all?

t's a matter of utilization. If you look across the competitive landscape, the other technology providers out there would largely say the same; we have tools, we have means of communication, we have the tools that we've made available to clients to be able to communicate recalls, new trades, collateralization requirements.

There's points of entry into the triparty world to transmit RQVs. We've got a lot of tools, clients need to make sure that they're adopting them fully. We encourage clients to talk to their counterparts, to their providers, to their technology vendors.

It does take an investment to build out and connect wherever possible, there's certainly the move in Canada to make some messaging interoperable through the working group, the catalyst set up.

It's all about sharing your pain points. We've got to identify where people have concerns and considerations and largely that's been around the recall space. Are the underlying beneficial owners getting cell notifications to their agent lenders quickly enough? Are those being able to be turned around into a generated recall that goes out to the borrowers quickly enough? When is that cut off time for notification going to stop? Is it 11.59? Is it market cut off? Is it governed by the underlying GM SLA that clients have in place between each other.

Ultimately, the market is going to continue to work relatively efficiently, you know, probably 95% of recalls are going to come back on time. The names that are problematic today are the names that are going to be problematic on May 29 of next year.

Equilend are introducing additional dashboarding, some screen redesign to try to identify potential problem areas more quickly and more readily and more easily. But generally speaking, the pipeline is there. The messages are running, we're generating something in the neighborhood of 125,000 trades a day. 40,000 returns a day. 1000 recalls a day are already flowing across steel pipes. It's on the industry to really adopt that technology and make sure it's implemented to its fullest

02 Given the 11:59pm cut off for recalls, how are firms setting up their staffing to handle recall processing and returns overnight in the US?

In the future, there will be a thorough evaluation of operating models and the potential benefits of additional location support.

Some firms will explore further utilization of existing APAC teams and handovers between regions will happen, occurring later in the US day.

Open dialogue with clients and borrowers will be maintained, aligning with the 11:59 best practice guidance. Recall notices will not be sent at 11:58 as that will certainly upset borrowers.

The central message will emphasize the necessity for efficient and prompt communication. When recall situations materialize, swift communication with borrowers will be crucial. Market service providers and available products will enhance efficiency. Despite potential late activities in the US day, a quick response will be essential, requiring strategic location planning as an integral component of the overall approach.

In the future, global agent lenders like Citi will rely on their existing infrastructure for leverage. The critical factor will be the timeliness of the messaging. Having quick visibility of sales notifications will be crucial. The faster these notifications are received, the quicker they can be processed within the platform. This rapid processing will enable lenders to make prompt decisions, such as allocation or issuing a recall. The emphasis will be on acting swiftly, without delaying until the latest point in the day. The goal will be to ensure efficient and immediate responses to sales notifications and related actions.
In the future, lenders will adopt various strategies. They will create pools of securities to act as a backstop in case recalls fail. Additionally, lenders may explore repo arrangements or reverse repos as part of their outreach efforts. There will be considerations about charging more for difficult-to-borrow securities. The recall process will be followed, but lenders will also expand their suite of offerings. These offerings will come with different price points based on the associated risk or complexity, as indicated by discussions with other lenders in the industry. This diversified approach will allow lenders to adapt to changing market conditions and manage risks effectively.

03 Doesn’t T+1 mean that we have to manage our inventory in real-time? Is there any alternative?

IIn the future, lenders will focus on positioning lending trades to potential borrowers and mitigating against recall cases. Handling recalls will be crucial, and some are well-prepared for the global nature of their business, unlike some other institutions.

The industry, including European firms, will transition toward real-time environments, although achieving 100% real-time inventory tracking, both within and outside firms, may not be immediately feasible.

Lenders will explore strategies such as maintaining pools of on-site securities for recall situations and creating collateral margin accounts.

Universal Transaction Identifiers (UTIs) will gain significance in securities lending, providing visibility and aiding in managing multiple borrowers.

Saphyre, in collaboration with Swift, will explore UTIs to enhance real-time technology across platforms. Interoperability will be a key focus, ensuring clients are not confined to a single solution.
Companies like Equilend and Broadridge will offer their solutions, contributing to a seamless industry approach.

04 What qualifies as T?

In the future, the recall process will be governed by contractual agreements between parties. The defined market cutoff, such as 4pm Eastern Time, will determine the timeline for recalls, making it crucial to adhere to the stipulated terms.

Currently, there exists a one-day lag between the recall due date and settlement sell date, except in cases where specific market arrangements or amendments are in place.

From a technical standpoint, if a recall request is received at 8pm, an instruction can be submitted until 9pm to take effect the next day.

However, the ability to act upon such requests will depend on existing agreements with counterparties and individual organizational policies. Decisions regarding the feasibility and implementation of recall instructions will be contingent on these agreements and the specific protocols in place within each organization.

In the future, most situations will proceed smoothly, with the majority of cases unaffected. The challenge will primarily arise in the tail names, those heavily shorted securities with limited supply. Retrieving these securities on time will be difficult, leading to potential issues. However, efforts will be made to return items promptly whenever feasible, but challenges will persist in specific cases, particularly those involving high demand and scarce supply.

05 What are the big risks in the T+1 recalls process? What issues should we be looking at ahead of time?

In the future, challenges in stock lending will primarily stem from potential breaks in Straight Through Processing (STP) at the core technology level.

These risks won't necessarily emerge today but will be a concern in the context of processing technology. Breaks in STP can impact stock ladders, affecting real-time updates and efficient matching. While real-time stock ladders are available, they won't be reliable if there are breaks in STP. To mitigate this, obtaining real-time information is crucial, coupled with dashboarding capabilities to identify STP breaks and address them promptly.

Although automation solutions, especially those driven by AI, will likely emerge, caution is advised regarding their immediate reliance.

Behavior and market dynamics in a T+2 market may differ from a T+1 market, requiring a cautious approach to automation. Over time, automation solutions are expected to evolve and mature, providing effective mitigants against the risks associated with STP breaks and ensuring readiness for real-time operations.

06 What tactics are you seeing for people to improve their access to collateral to support faster SBL?

In the future, addressing the contractual range arrangements will be a priority.

Firms will consider amending agreements and digitizing the process to have a comprehensive understanding of arrangements with various parties.

Digital solutions capable of amending and tracking agreements will play a crucial role in achieving seamless STP. Alongside digital advancements, existing market tools such as centralized collateral management and optimization tools will be leveraged.

Firms will establish arrangements for triparty collateral management with global custodians and explore options like collateral pools based on jurisdictions. Repo arrangements and reverse repos will be utilized for efficient management.

Real-time data dashboarding and reporting, stressed through rigorous testing, will be vital in understanding and handling the complexities of the new system. While Distributed Ledger Technology (DLT) represents the ideal state, its widespread adoption poses challenges.

Harmonizing parties on a single DLT platform and mapping data to blockchain technology are prerequisites. Although DLT offers the prospect of automated recalls and fulfilling obligations, the industry will focus on incremental steps, ensuring the right measures are taken and involving key stakeholders to achieve a comprehensive STP process.

07 Are we expecting to see a growth in brokers offering fails coverage lending after May 2024?

In the future, same-day activity across platforms will likely increase, indicating a shift toward real-time operations.

Having good inventory visibility will create opportunities, especially in the US. However, managing late-day cash activity, particularly for cash collateral, will pose challenges.

Redeeming or placing cash into reinvestment vehicles late in the day might stress existing systems. While there are historical challenges in this area, non-cash or tri-party solutions could become more valuable.

However, there are limitations on the extent of their implementation in the US. Demand for these solutions is anticipated, but their feasibility and effectiveness will need to be assessed as the industry moves towards real-time operations. Those with insights or experiences in this area are encouraged to contribute to the ongoing conversation.

In the future, the industry's uncertainty about the outcomes prevails, and any predictions remain speculative.

To tackle potential shortages, brokers could introduce additional offerings to subscribers, ensuring sales coverage.

Savvy opportunists are expected to seize this opportunity, leading to an increase in sales coverage provided by brokers in the initial months. This approach aims to create a safety net and enhance overall market stability during the transitional period.

08 Is T+1 going to impact lending liquidity for US and Canadian stocks - especially hard to borrow stocks?

In the future, as the industry approaches the go-live date, there will be a sense of trepidation among market participants.

People will be closely monitoring the situation, anticipating short-term challenges. These bumps are expected to smooth out quickly, driven by the resolution of any friction or uncertainty experienced by market participants during the initial phase.

If there is an increase in fails and asset owners perceive settlement risks in their portfolio trades, there might be a reduction in inventory.

However, the outcome remains uncertain, and it could go either way. It largely depends on how well the industry adopts the discussed themes and ensures overall readiness.

The market is described as a joined-up ecosystem, with collective preparedness across entities being crucial. If readiness is achieved universally, there is hope for a relatively seamless transition, although uncertainties still persist.

09 How are legal arrangements with my customers affected under T+1?

In the future, the industry will face a clear distinction between reality and potential problem areas. The key issue will revolve around contractual agreements, specifically the stipulated recall timings.

If there is a deviation from the agreed-upon recall time, such as issuing it at 9pm instead of the designated 4pm Eastern Time, problems might arise. However, these issues will only be significant for a limited percentage of cases, approximately 5%, governed by the individual contracts between counterparties.

Compliance with best practices will be essential, yet the real challenge emerges when multiple parties, including conduits, are involved.

The resolution will depend heavily on individual counterpart pairs and their adherence to contractual agreements and best practices. Despite the industry's efforts to establish standardized practices, ultimate protection lies within the terms outlined in each contract.

In the future, managing the compressed timelines in the industry will be challenging. With limited time, dealing with the nuances of gray areas becomes difficult, especially when there's a psychological hesitancy to issue a recall only after the settlement date of the underlying sell.

This issue has garnered significant attention, prompting discussions about eliminating gray areas. Despite the industry's heavy reliance on relationships, efforts are being made to establish clear guidelines. Industry conversations play a crucial role in defining best practices and contract implementations.

However, reaching a consensus remains uncertain. It is imperative for industry players to engage in open dialogues, sharing insights about potential issues. Collaboration with internal risk and legal teams is essential to ensure comprehensive coverage in contracts, addressing concerns and minimizing uncertainties as much as possible.

10 What questions should I be asking of my agent lenders to make sure that they are ready for T+1?

Focusing on enhanced communication strategies with agent lenders will be crucial to adapt to the T+1 environment.

Investors should inquire about the steps taken by lenders to reduce timescales and improve efficiency. Utilizing technologies such as APIs and shared platforms will play a vital role, emphasizing the need to move away from traditional methods like email communication.

These inquiries, along with discussions about fees and agreements, should be part of the evaluation process when selecting an agent lender. The industry's push toward T+1 is seen as a positive move, promoting market efficiency. However, achieving this goal will heavily rely on technological advancements rather than solely increasing manpower.

Investors should be encouraged to actively engage with lenders, seeking systematic solutions that facilitate T+1 lending processes and enhance overall efficiency.

11 Will fines actually be an incentive for change in Europe?

The effectiveness of regulations such as CSDR in improving fair rates remains uncertain, with no conclusive empirical evidence yet.

The regulator's potential response to this situation is a topic of ongoing discussion. While fines might not necessarily lead to improved behavior, there is consensus on the need to focus on operational resiliency.

This concept is divided into two key aspects. Firstly, there's a need to redefine the Target Operating Model (TOM) and operational workflows, emphasizing the importance of a comprehensive refresh. Secondly, the industry is increasingly prioritizing technology resiliency, especially in post-trade operations.

Traditionally, technology resiliency was associated with the front office, but now, there's a significant shift towards post-trade functions, including insurance settlement cycles.

This shift is driving the implementation of sophisticated resiliency measures, such as full replication and Hot Standby configurations between primary and secondary sites. The demand for enhanced technology resiliency is growing, necessitating a more comprehensive and advanced approach to ensure the stability and reliability of post-trade operations.

Fines may have a limited impact on encouraging adoption within financial institutions. While fines might instill fear and promote awareness, true progress hinges on the industry's ability to adopt standardized tools and technologies.

Many firms already possess their own tools, and some of these tools offer visibility across different entities. However, the effectiveness of these tools depends on the industry-wide adoption rate.

The challenge arises when one institution is technologically advanced, but its counterparties lag behind. In such cases, the industry's overall progress slows down, akin to a dance class where the pace is determined by the slowest participant. The question regarding hard-to-borrow securities was raised in the chat, presenting an opportunity for further discussion.

12 What should people be doing to test ahead of May?

In preparing for the future, organizations should start by defining their Target Operating Model (TOM) and clearly understanding the operational changes necessary to align with it.

It is crucial to have a well-defined TOM before considering what to test. Therefore, organizations should focus on answering the question: "What's the model you should be testing against?"

Once the TOM is established, organizations can proceed to determine how to test it. Collaboration with partners and counterparts, particularly lenders, is essential. Communicating the operational changes and requirements derived from the TOM to counterparts will facilitate effective testing processes. This proactive approach ensures that testing efforts are purposeful, aligned with organizational goals, and conducted in coordination with relevant stakeholders.

13 What extra steps should a London based securities borrower or lender of US or Canadian equities take if recalls may come in during the evening of trade date?

In preparation for the T+1 transition, you'll need operational teams available, particularly in May, June, and July of 2024. Initially, these teams may be located in relevant locales or in the US to closely monitor the ebb and flow of trade flows. As you gain a better understanding of these patterns, you can consider transitioning to a more streamlined team. It's important to upgrade your infrastructure to be responsive as well, but the operational setup remains similar for non-US teams.

When selecting a lending provider, prioritize those with a large-scale book that can reallocate securities without the need for recalls. Key considerations include the breadth of their book and their scalability. For instance, some plan to utilize their Singapore desk for US recalls. Look for vendors that offer automated recall processes with borrowers. Collaborate closely with your vendors, partners, brokers, dealers, and counterparties to ensure readiness and alignment with the evolving landscape.

14 What assurances can we provide for beneficial owners that T+1 overly negatively affects their securities lending performance survey?

The fear regarding hard-to-borrow securities might be alleviated by the measures discussed in this panel. Agent lenders can address this concern by diversifying how these securities are lent out, placing a premium on them, and establishing backstops such as jurisdictional collateral pools.

The key lies in the arrangements made with borrowers and understanding the chain reaction effect of multiple borrowers, especially concerning potential recalls.

If these comprehensive strategies and precautions are in place, lenders can provide assurances. However, if such measures are lacking, there might be a reconsideration of lending these securities. This perspective underscores the importance of proactive and well-thought-out lending strategies to manage the challenges associated with hard-to-borrow securities in the future.