



Minutes

Securities Lending Committee

20 November 2018

Location: Bank of England, Threadneedle Street

Attendees:	Prudential	Nina Moylett (Chair)
	Aberdeen Standard Investments	Matthew Chessum
	Aviva Investors	Mick Chadwick
	BlackRock	Tim McLeod
	BoNY Mellon	Staffan Ahlner
	Citadel	Timothy Tomalin-Reeves
	Citi	Andy Krangel
	Clifford Chance	Habib Motani
	Goldman Sachs	Mark Short
	HSBC	Jamie Anderson
	ISLA	Andrew Dyson
	Lloyds Bank	Jamie Smith
	Morgan Stanley	Krishan Chada
	Norges Bank Investment Management	Matthew Brunette
	Prudential	Simon Dunderdale
	State Street	Alex Lawton
	DMO (Observer)	Jessica Pulay
	FCA (Observer)	Alessandro Puce
	ICMA (Presenter)	Andy Hill
	BoE	Iain Ramsay (Secretary)
	BoE	Jonathan Pyzer
	BoE	Rhys Phillips

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1. Introduction

Nina Moylett (Chair) welcomed Andy Hill (ICMA) Alessandro Puce (FCA) and Rhys Phillips (Bank of England) to the meeting.

2. Market Update

ISLA gave an overview of their recent market deep dive, following which a number of prevailing themes were discussed.

On the supply side, the availability of securities for lending had increased and lending balances had increased to in excess of \$2 trillion globally. ETFs were seen as a particularly rapidly growing source of new securities for lending, and SWFs retained their position as a key source of supply. Idiosyncratic supply drivers identified included the underlying strength of equity markets as well as the general system-wide level of leverage. The outlook for global QE could be a changing structural dynamic on the supply side in 2019.

Regulatory changes were expected to be an important driver of the outlook for the securities lending market. The committee had previously discussed how increased transparency due to SFTR would likely alter the level of participation by SWFs in particular. The implementation of

NSFR could also change the balance of how assets are funded. The outcome of Brexit for financial services would determine the extent to which collateral pools may or may not become more disjointed.

Members also discussed fails. CSDR was expected to focus attention on the issue of fails, which was broadly seen to have increased in prevalence. Specific issues raised included the exposure of securities lenders to the potential issue of unpaid dividends in default, an area of post-trade believed by some to not be sufficiently closely focused on. Some members were concerned that a 'chain of fails' was often created by one fail, and that some fails could not be prevented as an earlier fail simply meant that appropriate securities were not available for delivery. So reducing initial fails would have a multiplier benefit in reducing follow-on fails more widely.

3. Market impact of CSDR

The Chair reminded members that the Committee Terms of Reference states that one of the SLC's objectives is to discuss market developments including those of a regulatory nature, and therefore this agenda item was not intended to be a lobbying opportunity

The FCA provided some background and update on the current position with regard to the introduction of CSDR. ICMA presented to the Committee on CSDR with a focus on potential issues related to mandatory buy-ins. The buy-in mechanism in the CSDR text could produce potentially asymmetrical outcomes as the economics of an original trade would be impacted by a buy-in depending on whether it takes place at a lower or higher price than agreed in the original trade. In a falling market the buy-in payer is penalised and the receiver benefits, whereas in a rising market the economic impact is neutral. The industry is seeking to establish a potential contractual change which could address this asymmetry. Other issues raised included the implications for existing legal documentation e.g. GMRA and GMSLA, and the possibility of a buy-in agent not being found.

Members discussed *cash* buy-ins and the risk that funds could essentially become disinvested. This would be expected to be a greater issue in less liquid markets due to lower stock availability. Implications of the implementation of buy-ins on the securities supply side was also discussed as members saw the possibility of perceived higher risks for securities lenders (due to the asymmetry and potential for economic loss in the case of failing a trade) resulting in higher rates demanded or a reduced universe of securities for lending. This would naturally be additionally problematic for securities where the lending market is already relatively illiquid.

4. Update on SFTR

ISLA provided a brief update on SFTR. There was general acceptance that SFTR had become a fact of life; it was thought to have some benefits in making the industry review how it recorded and maintained data. Indeed SFTR was considered beneficial that the initial hurdles of implementation were gradually being overcome as it provided a far cleaner and more usable data set. There were some negative aspects highlighted in terms of costs. It remained to be seen whether SFTR have any impact on non-regulated entities continuing to trade.

5. Update on Pledge Structures

ISLA noted that GMSLA documentation for pledge transactions had been completed. Clifford Chance gave a summary of the new documentation it had developed. It was stressed that the documentation would reflect that of a typical pledge transaction that would not allow rehypothecation of the securities. It was noted however that some sectors of the market at this point remain unable to use pledge structures, including for example many UCITs funds. Pledge and title transfer were therefore expected to co-exist.

6. AOB

The Committee discussed topics for its forward agenda for 2019. Discussion items at future SLC meetings could include inefficiencies in the securities lending trade life-cycle and potential solutions to these; tools to demonstrate best execution/relative performance management; Basel IV minimum haircuts; the impact of ESG on securities lending; and impact of data on securities

lending including from SFTR e.g. on optimisation of securities inventory.

Dates for 2019 meetings of the SLC would be confirmed in due course. The Committee agreed that they should meet three times in 2019 including one meeting to hear from external presenters.