BANK OF ENGLAND

Securities Lending Committee

Minutes

04 February 2021

Time:	14:00 – 15:30
Location:	Conference Call

Attendees

Ben Goodsell	Aberdeen Standard
Matthew Chessum	Aberdeen Standard Investments
Adam Jacobs-Dean	AIMA
Mick Chadwick	Aviva Investors
Ina Budh-Raja	Bank of New York Mellon
Andy Krangel	Citi
Caroline Dawson	Clifford Chance
Habib Motani	Clifford Chance
Jack Skinner	DMO
Jo Whelan	DMO
Charlie Graham	FCA
Alan Barnes	FCA
Johanne Armita	Goldman Sachs
Shikha Kalra	HSBC
Godfried de Vidts	ICMA
Andrew Dyson	ISLA
Harpreet Baines	JP Morgan
Guy Rolfe	M&G
Simon Dunderdale	M&G Plc
Nina Moylett	M&G Plc (Chair)
Krishan Chada	Morgan Stanley
Matt Brunette	Norges Bank Investment Management
Alex Lawton	State Street

Apologies

Jon Pyzer	Bank of England
Tim McLeod	Blackrock
Tanja Hauenstein	Credit Suisse
Alan Barnes	FCA
Wladimir Kraus	FCA
Joana Barata	Goldman Sachs
Jamie Anderson	HSBC

Bank of England

Rhys Phillips
Paul Alexander
Shashi Daboo (Secretary)
Nicole Webster (Secretary)

Item 1. Bank of England Introductory remarks and minutes from last meeting

The Chair welcomed Caroline Dawson, Guy Rolfe, Ben Goodsell and Shikha Kalra as part of the Bank's initiative to make such meetings more diverse and inclusive.

The Chair confirmed that the minutes of the November 2020 meeting were published on the Bank of England's (BoE) website.

The Committee had no comments to raise on the minutes from November's meeting.

Item 2. Recent market trends and observations

The Chair introduced a discussion on recent market conditions and trends. It was noted that following a drop in activity at the height of the Covid-induced crisis In March/April 2020, volumes and exposures in Securities Lending had rebounded in the second half of 2020.

2020 year-end was fairly stable for most members with some viewing it as a 'non-event'. The increase in volumes over year-end were predominantly in non-cash collateral driven in turn by demand for asset-swap-type transactions. Members agreed that the market was well prepared for the 2020 year-end turn.

Activity in Fixed Income collateral was elevated into the turn with equity collateral volumes stable. The moves in Fixed Income were driven by widening cross-currency swap spreads and equities versus government bond trades. The increase in gross balances over year-end were driven by cross-currency swap transactions (55% of the increase), and government bonds (45% of the increase). Members observed increased Hedge Fund activity into year-end as some loss-making short positions were closed out.

Members noted that liquidity levels were currently good, with a strong availability of both high-grade and low-grade collateral. Liquidity overall was in line with pre-Covid levels.

Some lenders noted an increased appetite to broaden collateral types in a bid to secure additional yields.

The global recovery in H2 2020 supported by monetary and fiscal stimulus had helped boost equity valuations which in turn supported gross exposures through long-equity positions rather than shorts. Volumes were supported by capital-raising, and balance-sheet restructuring.

Looking to 2021, many of the themes from 2020 are expected to continue. It is anticipated that restrictions on travel will remain in place, members expected an uptick in M&A activity and corporates are expected seek to maintain/increase cash reserves. SPACs issuance is anticipated to develop further in Europe following growth in the US in 2020.

Item 3. Future Landscape – Brexit, Biden and wider structural impacts on Securities Lending Markets

Members noted that the future landscape will continue to focus on clearing regulatory hurdles e.g. NSFR, LCR and RWAs.

Some members suggested that securities lending in the Middle-East e.g. Saudi Arabia and Kuwait may present some opportunities.

In the US, focus may turn to the potential reflation trades as a result of the Biden administration - that could in turn, impact the desire to hold US dollars. Other members felt that developments through US broker-dealers accepting non-cash collateral would garner more focus in 2021.

Some members identified that the Hedge Fund community had seen positive inflows for the first time in a while. Overall, gross exposures were high and expected to continue to grow with activity anticipated in the rotation out of technology stocks and into more international assets.

Members agreed that creating European entities had been an orderly exercise. But the challenge going forward would be to decide on those assets to be booked into the European entities. More consideration would be needed in the future on the RWA impact of trading out of the UK versus Europe. Clients were waiting to see what equivalence will look like before acting. In the interim, the market would look to adapt to the new (post Brexit) set-up and seek to make efficiencies where possible. Other members felt that equivalence would not happen, with risk weights on UK exposures currently applied on the basis of no equivalence.

Members talked about the recent moves in Gamestop and the surge in retail trading activity. Concerns were shared about the short-selling headlines emanating from some of press coverage of these moves. Members expressed their disappointment that the benefits of short-selling and lending for price discovery and market liquidity were being drowned out by negative headlines on short-selling. There was discussion on whether the regulators e.g. FCA should make a public statement on the benefits of short-selling and securities lending to the market. Members unanimously agreed that a lot of time and resource had been deployed in educating regulators and market participants on the benefits of securities lending and short selling. There was concern that all this work could be undermined by the recent activity and associated press and social media coverage. Some members were worried that the discussion on securities lending was moving out of the economic arena and into the political one. Members shared their frustration that the securities lending industry was coming under criticism yet there was no medium or mechanism through which the industry could counter those arguments. It was agreed that discussion on this topic would continue at the next meeting.

Item 4. Environmental, Social and Corporate Governance (ESG) in Securities Lending Markets

Members agreed that the ESG credentials for securities lending had made big strides forward over the previous 12-18 months.

Differences in the US and European views of ESG were discussed. It was noted that in US ESG concerns are tied towards better management of risk while in Europe ESG considerations were targeted at changing behaviours and whether this could lead to different geographical approaches with regards to the ESG and securities lending.

It was noted that ‘green’ repo was growing in volume, and that securities lending would provide a crucial role in improving liquidity for those markets. Members agreed that this year would be important for ESG in securities lending. One member shared that 8 out of 10 investment dollars were being deployed with either State Street, Vanguard or Blackrock –with all three asset managers placing increased focus ESG investing.

Members debated whether voting rights or income on securities would become more important for their clients. Some members expressed the view that some fund managers were keen to recall stock to allow them to vote. There was consensus that decisions on voting rights would become more important for ESG going forward. Other members shared a concern that if an increasing proportion of stock owners sought to retain voting rights then this could cause liquidity squeezes in specific stocks. Others noted that some Fixed Income clients had reviewed their firm’s voting records and were interested to see how their firm had voted on ESG issues.

Concerns about the general optics of short selling in non ESG stocks were raised again and specifically whether in the case of a 'green-type' company subject to short selling this could create negative press for the securities lending industry on its ESG credentials.

Item 5. UK Money Markets Code

The Bank of England provided an overview on updates to the Money Market Code.

Over 200 firms had signed up to the code. The Money Markets Committee had committed to keeping the code up-to-date, a process that had been led by market participants and executed through a number of working groups.

The Money Markets Committee unanimously agreed to these updates, agreeing that they were both progressive and relevant with the key updates incorporated into the Code and this was signed off in December 2020.

Existing members would not need to re-sign up to the updated Code.

The idea of proportionality was more in the forefront of the updated Code. The preamble to the Code now promotes a more diverse and inclusive team. ESG considerations are brought into the code, and the Code is now less prescriptive on ways of working. Settlement discipline is now more clearly explained in explanatory note and FAQ section.

Plans to publish the updated Code have been revised. Initially the updated Code was to be published near the start of 2021, but this has now been revised to April 2021.

Item 6. Diversity and Inclusion on Securities Lending Markets

The Chair invited any updates or thoughts for future meetings regarding D&I.

Members agreed that a recent industry event on D&I had proved extremely valuable. Concepts like intersectionality that are really important in trying to build inclusive cultures had received a lot of attention. It was agreed that consideration would need to be given to what the post-Covid work environment will look like, employees' expectations on what the future work-place would look like have changed in the last year.

Item 7. AOB

Results of analysis on settlement discipline were shared with the Committee. The analysis aimed to understand why so many fails happen in the night settlement cycle. It was discovered that some firms purposely held onto their settlement instructions until the end of the day as a result of liquidity regulations that may encourage some firms to smooth out their liquidity demands over the day. Further analysis will be conducted, with the ECB expected to comment on this issue on 29th March.