THE NETWORK FORUM JOURNAL

Connecting Financial Institutions Worldwide

Issue 8

Contents

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THE NETWORK FORUM

Welcome

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It's been a little while since I wrote the opening editorial to the TNF Journal, and in some ways a great deal has happened since then, and in other ways it hasn't. The pandemic has made us re-evaluate and review many established working practices, but at the same time brought many things to a complete standstill. Many things have had to change, but others have remained the same. What is clear is that our industry has functioned, and continues to function, to a comparable degree during the pandemic as it did before, and – if it isn't premature to say so – as we emerge from the other side of it. Ongoing evidence, if any more were needed, of the resilience of the global financial system, as the pace of digital innovation continues to increase exponentially...

As many of you will now know, TNF will be holding it's first "in person" gathering in almost two years in London on 3rd of November, and to say we cannot wait to get back in a room with our community would be an incredible understatement - and something to which we know you can all relate. I honestly cannot remember the last time I was this excited about anything – sad, possibly, but very true!

But on to more editorially focused matters: What can you look forward to within the pages of this latest Journal? The simple answer is: Even more of what you have grown to expect and hopefully enjoy!

For starters, as Mental Health Day was only a couple of weeks ago and psychological well-being is without doubt a year-round concern, we have some notes on building resilience through self-awareness by Anna Lewczuk, who is making it her mission to tackle this head-on after a decade in the financial services industry.

Elsewhere, we have articles on accelerated settlement and the move towards T+0 – a very hot topic which we explored during our recent Americas Meeting and will be revisiting on the agenda of our Asia Meeting in a few weeks' time.

Also, GBST talks to TNF about legacy post-trade systems and how they compare with the flip-phone of the early 2000s: and why implementing a modern, cloud-based middle- and back-office platform should be viewed in the same way as using a Smartphone in 2021.

And there is much more besides.

So, dear reader, do enjoy this edition of the TNF Journal, and it does feel truly amazing to be able to say this again – we look forward to seeing as many of you as possible on the road in the weeks and months to come!

Edward Jones

Managing Director

The Network Forum

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The Network Forum are honoured to be supported by The Founding Partners below.

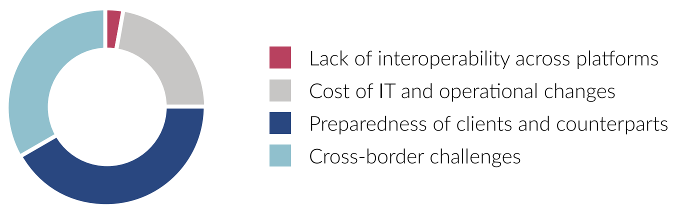
TNF Americas – Key Takeaways

Although the Americas have been hit disproportionately hard by COVID-19, a recovery – albeit a slow one – does appear to be underway across the majority of countries. As markets gradually normalise, the securities services industry – having navigated the pandemic - is now looking towards the future.

Taking settlements to the next level

What was historically considered by some to be one of the more unglamorous aspects of the investment lifecycle, trade settlements have been thrust into the forefront of people's consciousness following recent market events. A combination of the unprecedented COVID-19 volatility in March 2020 together with the meme stock trading debacle – whereby retail investors, influenced by social media chatrooms, piled into cheap, unfashionable securities en masse leading to extraordinary price fluctuations – have given credence to those pushing for a T+1 settlement cycle for equities. The DTCC is making the case for T+1, highlighting that shorter settlements will mitigate settlement risk, and could also free up capital and liquidity as traders would benefit from reduced margin calls. While the US is pushing ahead with its move to T+1 – and could even implement it by as early as 2023, some South American markets are less convinced by T+1's merits, especially as several of them have only just transitioned to T+2. Critics of T+1 point out it could create logistical problems because of the time zone differences between various markets and the need to book FX transactions on a same day-basis.

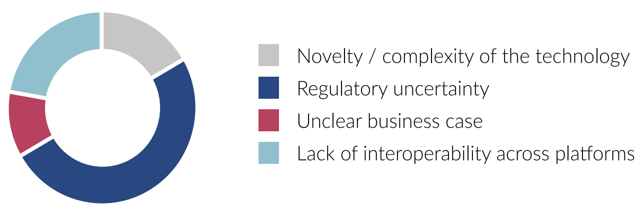
Audience poll: What are you most concerned about in the move to T+1?



Progress on digitalisations continues

With physical interactions on hold [in most countries], market participants were forced to digitalise their operations, especially in areas such as corporate actions and proxy voting. Longer-term, providers are assessing how they can integrate DLT [distributed ledger technology] and APIs [application programming interfaces] into their business models. This is easier said than done, not least because there is a lack of consistent regulation and commonly-agreed upon standards underpinning these technologies. Without a semblance of standardisation to facilitate interoperability, adoption of these technologies will be limited. Just as the post-trade world embraced dematerialisation of physical securities almost 25 years ago, the emergence of digital assets is considered to be the next stage of the industry's development. Regulators in the US – including the Securities and Exchange Commission [SEC] – are likely to introduce greater oversight of digital assets. A combination of sensible regulation together with the growing willingness of bank custodians to provide safekeeping will help generate interest in digital assets among institutional investors. However, there are concerns in some quarters that the US is likely to take a tough line on digital assets, particularly after the SEC's nasty tussle with Coinbase over its plans to unveil a crypto-lending product.

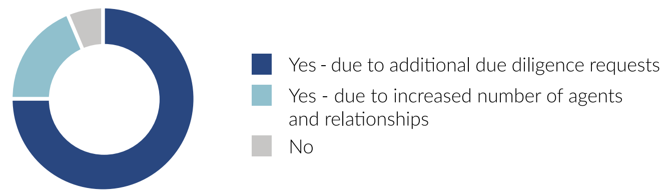
What is the biggest barrier in capital markets to adoption of blockchain technology?



Network managers continue to evolve

As custodians and broker dealers look to deliver efficiencies in the due diligence process, network managers continue to leverage the AFME DDQ, although some sub-custodians complain clients are tagging excessive numbers of questions onto the document – a recurrent criticism at TNF for many years now. Post-COVID-19, network managers are ramping up their scrutiny of agent banks' operational resiliency and cyber-security measures, although some believe network managers are ill qualified to be asking questions about these subject matters. Elsewhere, due diligence on cash correspondent banks is on the rise. Fuelled by CFTC [Commodities Futures Trading Commission] and OCC [Office of the Comptroller of the Currency] requirements in the US, banks are being forced to conduct more rigorous assessments of their third party providers including cash correspondent banks.

Cash correspondent - Have your responsibilities been augmented in the last couple of years to include monitoring of your cash correspondent agents?



Charles Gubert
Founder
GTL Associates

The Evolution Of Custody In Latin America

Throughout Latin America, the continued uptick in retirement savings is expected to help boost domestic AUM by more than 10% annually through 2025, according to recent data from PwC.[1] With investment guidelines becoming less restrictive, pension managers in countries like Mexico, Peru and Chile have steadily increased their cross-border allocations (which, all told, rose some 19% in 2019, notes Cerulli Associates).[2]

Meanwhile, alternative strategies such as infrastructure, real estate and private equity are likely to assume greater prominence in regional pension programs going forward, with IMF, Lipper and other observers forecasting a two-fold increase in alternative AUM over the next four years. In the two years since Mexico's AFORES Pension System authorized investments in global alternatives, such allocations have nearly doubled, closing 2020 at nearly $10bn in capital commitments, according to data from BMV Group.[3]

With greater participation comes the need for greater transparency into investment fund flows, putting added pressure on managers to keep pace with current solutions and protocols. Bolstering competencies in areas like trade execution, portfolio analytics and other compulsory services can be a costly proposition, however, particularly for smaller funds only now getting up to speed in terms of front-to-back office efficiency.

Accordingly, a growing number of asset managers are seeking all-in-one, third-party platforms capable of handling an increasingly sophisticated array of fund activities. The Latam pension expansion will have a measurable impact on regional custody players as well.

Custody to the Rescue

Despite being among the globe's hardest-hit regions due to COVID-19, data from the Economic Commission for Latin America and the Caribbean (ECLAC) pegs current-year growth at around 3.7%, as local economies gradually begin to reopen.[4] Maintaining that trajectory will require that governments continue to expand fiscal and monetary policies, while also promoting greater investment in sustainable programs and practices.

A decade after establishing its first Latam-facing custody, clearing and administration platform in Brazil, BNP Paribas continues to seek growth opportunities in the region. When managed effectively, custody drives portfolio efficiency, offers security to investors through better risk controls, and provides an operational and technological infrastructure in support of funds' growth strategies. At BNP Paribas, for example, all custody and settlement services are supported by Neolink, a tool that ensures accurate processing of trade instructions to the custodian, as well as the interactive data navigation analysis tool DNA, capable of delivering highly granular risk and performance analysis even when dealing with massive volumes of data.

It is a time of great change within Latin America, marked by the emergence of newer asset classes such as ETFs, as well as ongoing innovation and digital transformation. For providers with the right skills, solutions and regional presence, there will likely be opportunities aplenty to help Latam pension managers achieve the kind of streamlined trade processing and investment transparency that their clients require.

Claudia Calderon,
Head of Colombia & Hispanic Latam
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Luis Fernando Barahona,
Head of Asset Managers Latam & Asset Owners Americas
BNP Paribas Securities Services

BNP PARIBAS
The bank for a changing world

1. PWC report, "Asset & Wealth Management Revolution," Jan. 2021
2. "The Cerulli Report—Latin American Distribution Dynamics 2020: Emerging Opportunities in Uncertain Times," Dec. 2020
3. Source: BMV, BIVA, Sept. 2020
4. ECLAC report, "Preliminary Overview of the Economies of Latin America and the Caribbean," Feb. 2021

MENA Stages A Comeback

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While the pandemic caused an initial sell-off in emerging markets – including MENA [Middle East, North Africa] - the region quickly recovered and it is now witnessing exponential global investor inflows. In addition to the attractive returns available in MENA, the region is also implementing overarching reforms of its capital markets, embracing global best practices and digitalising pre and post-trade processes to encourage liquidity back into the region.

Investors Return to MENA

With interest rates in developed markets at historic lows, investors are seeking superior returns by building up their exposures to emerging economies. "Since the last quarter of 2020, MENA markets – especially those with a reputation for sensible economic management and limited currency and interest rate volatility - have been seeing healthy inflows," commented Gunsel Topbas, Head of Securities Services, EMEA Emerging Markets at Citi.

"Global institutions in Europe and North America have been trading Egyptian securities for a long time now. However, they have started relatively recently investing across the GCC [Gulf Cooperation Council] countries. We have also observed that more Chinese institutions are now investing into emerging markets such as MENA," continued Topbas.

Inflows into the GCC - principally Saudi Arabia and Kuwait - have been facilitated by index inclusion, a development which has resulted in a number of passive providers and mutual funds increasing their exposures to both countries. Saudi Arabian stocks were added to the MSCI Emerging Market and the MSCI ACW indices in 2019 while FTSE Russell incorporated the country onto its global equity index series in 2020. Foreign holdings of listed equities now total $60.9 billion in Saudi Arabia, a significant increase since 2015 [1].

Meanwhile, Kuwait also joined the MSCI Emerging Markets Index in 2020, in what lead to an additional $3.1 billion of foreign capital moving into the country [2]. These inclusions come almost seven years after both the UAE and Qatar were upgraded to Emerging Markets status by MSCI.

Liberalisation and Market Enhancements Drive Inflows

The decision by major index providers to add Saudi Arabia and Kuwait to their benchmarks is a reflection of the positive market reforms which these countries have adopted over the last few years. Since first opening up its capital markets to foreign investors six years ago, Saudi Arabia's regulator – the Capital Market Authority [CMA] – has continued to ease restrictions on inward investment on both the Tadawul, the country's main stock exchange and Nomu, its parallel equity market.

Whereas previously, qualified foreign investors [QFIs] could only access the local Saudi Arabian market if they had at least $5 billion in AUM [assets under management], this threshold has since been revised downwards to $500 million. The CMA has also stepped back from authorising QFI applications, and is delegating the task to AAPs [authorised assessing person] – namely custodian banks, in what is helping to expedite the QFI approval process. "In addition, Saudi Arabia has eased its foreign ownership restrictions and simplified investor disclosure requirements. By doing this, the country is aiming to generate greater foreign interest in local IPOs [initial public offerings] and secondaries," noted Topbas.

GCC Countries are also introducing more investment tools for foreign institutions by creating markets for securities lending and borrowing, and derivatives. Investor protections have also been strengthened through the establishment of central counterparty clearing houses [CCPs] in the region. The Tadawul in Saudi Arabia not only launched a derivatives market but it also established a CCP – known as Muqassa. Similarly, regulators in Kuwait and the UAE [Abu Dhabi Exchange and Dubai Financial Market] are all launching their own CCPs. By setting up CCPs, these markets are demonstrating their commitment to best practices.

Other liberalising measures include Kuwait's decision to harmonise its settlement cycle for local/foreign investors to T+3, and its introduction of delivery versus payment. These progressive initiatives are playing an integral role in encouraging foreign investment into MENA - facilitating greater diversification and deepening market liquidity.

The Improvements Keep Coming

Historically, one of the main challenges precluding investment into MENA was the absence of harmonisation, especially around market access and account openings. The account opening processes in individual MENA markets were often quite different, creating inefficiencies for foreign investors. Nevertheless, this is changing as account openings – along with other processes – are becoming less complicated than what they once were as a number of MENA markets adopt internationally accepted best practices. This is ultimately leading to reduced fragmentation.

The pandemic has also prompted MENA markets to embrace digitalisation and move away from manual, paper-based processes in activities such as account openings, corporate actions and proxy voting. Not only does this reduce the risk of errors happening, but it makes it much more efficient for investors when entering the market. It is widely believed that these digital changes will stay in place post-pandemic.

Corporate governance has also undergone marked improvements in MENA, having traditionally been an area of concern for many foreign investors in the region. "Enhancements to governance in MENA are being driven by foreign investors, many of whom are taking a growing interest in matters related to ESG [environment, social, governance]," noted Topbas.

Institutions – especially those based in the EU and UK – are coming under mounting pressure from regulators [along with their own underlying investors] to integrate ESG into their investment processes. For example, the UK and EU both now require institutions such as asset managers to disclose how they incorporate ESG into their investment and risk management activities. This is having a downstream impact in terms of how they invest in emerging markets such as MENA.

MENA on the Ascent

A combination of the strong return potential in emerging markets, together with ongoing market liberalisation initiatives, digital transformation; and adoption of best practices are all helping the MENA region attract greater inflows. Most significantly, these markets show no sign of slowing down with their liberalisation and digitalisation agendas. Although it is very unlikely MENA will follow the EU's footsteps and develop standardised cross-border regulation – or even consolidate its FMIs [financial market infrastructures], the region is set to continue adopting global best practices to the benefit of international investors, which in turn will continue attracting portfolio investment flows.

Gunsel Topbas,
Head of Securities Services, EMEA Emerging Markets,
Citi

1. Institutional Investor [September 14, 2021) The transformation of Saudi Arabia's stock exchange offers compelling opportunities for investors
2. Arabian Business [November 30, 2020) Boursa Kuwait sees $3.1 billion inflows after MSCI upgrade

TNF Annual Review – Message From A South West London Suburb

Despite all of the upheaval over the last 18 months, the securities services industry has not only weathered the strain of the pandemic, but it adapted quickly and continues to innovate. Experts from across the world gathered online for the Network Forum's (TNF) Virtual Annual Meeting between June 30 - July 1. Charles Gubert, founder of GTL Associates, takes a look at some of the main talking points.

Don't bet on a return to the old ways of doing things

Attendees at TNF seemingly accept that the traditional modus operandi of the securities services industry is unlikely to return. Gone are the days of when international travel used to be synonymous with the role of network managers and sales executives. As more financial institutions attempt to rein in costs and scale back on their CO_2 emissions, travel budgets are likely to come under significant pressure. In place of quarterly or annual face to face meetings with international clients, experts anticipate communications will become virtualised albeit more regular. Similarly, speakers also noted that virtual AGMs (annual general meetings) – which were permitted by regulators during the peak of the pandemic – are likely to be retained post COVID-19 owing to their success. However, that is not to say in-person meetings or international conferences will become a thing of the past. One executive added securities services is an inherently people-driven industry which thrives on human connectivity.

Crypto is still all the rage

As more institutional investors dip their toes into crypto-asset trading, the securities services industry is being forced to respond. Security – or lack thereof- was historically one of the biggest barriers precluding institutions from touching crypto-assets. The decision by some custodians, however, to develop highly secure and regulated crypto-custody solutions could mark a turning point and provide a level of comfort to risk averse investors. Elsewhere, regulation of digital assets – at least in the EU – is gathering momentum following the publication of the Regulation on Markets in Crypto-assets (MICA) bill. Most strikingly, the rules clarify what the EU believes to be unregulated (i.e. crypto-currencies) versus regulated digital assets (e.g. security tokens). In the case of the latter, MICA will establish a pilot regime allowing for market infrastructures to support the trading and settlement of crypto-assets using distributed ledger technology (DLT). Although MICA is supposed to come into force in 2022, experts reckon it could be delayed until 2024 - by which time it will probably be out of date.

Regulations to watch

Aside from MICA, there are a number of other regulations likely to impact the industry much sooner. TNF attendees are optimistic there could be a reprieve on the Central Securities Depositories Regulation's (CSDR) Settlement Discipline Regime, principally around the rules concerning mandatory buy-ins. After months of warning EU regulators that mandatory buy-ins could have serious implications on market liquidity and may even potentially inflame systemic risk, experts are confident the authorities could make buy-ins voluntary when the rules take effect next year. Elsewhere, one speaker urged the TNF audience to pay close attention to the EU's Digital Operational Resilience Act (DORA), as it will impose tough operational resiliency requirements on financial institutions. Under DORA, banks must demonstrate they have oversight of their critical third party IT providers – a risk which has become increasingly important - following several well-documented technology outages.

Data – an uphill battle

Despite the industry's commitment to strengthening its data sharing capabilities and quality, almost two thirds of network managers told a TNF survey that they received less data than what they needed. This is a problem which has been exacerbated by the absence of data standards. With sub-custodians operating across a number of different and often unique markets – together with network managers requesting data that is tailored specifically for them – standardisation is likely to be a major challenge.

See you next time….

After a thoroughly successful and enjoyable Virtual Annual Meeting, TNF will once again return in-person (we hope!) at the TNF Annual Meeting in Warsaw next June 2022.

Charles Gubert

Founder,
GTL Associates

Building Resilience Through Self-Awareness

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Have you ever felt overwhelmed at work? Have you felt like life has been happening TO you, not FOR you?

A 2019 Gallup study showed that 76% of full-time employees experience burnout on the job, at least sometimes. Furthermore, if you belong to this group, then you are:
- 63% more likely to take a sick day
- 23% more likely to visit the emergency room
- 2.6 times as likely to be actively seeking a different job.

Speaking from experience, I believe this is due to losing touch with ourselves while feeling a strong dissonance and lack of integrity between our core values and what we experience and witness at work.

Many have already decided to quit the corporate world. I believe this isn't the only solution.

Why self-awareness underpins personal success and growth

Countless studies show that people who are more self-aware are more fulfilled, creative, self-empowered and confident. They have stronger relationships and are better communicators. They're less likely to lie, cheat and steal. They perform better at work, are more promotable and are more effective leaders with more profitable companies.

It's also been found that there are two types of people: those who think they are self- aware (around 85-90%) and those who really are (10-15%), as verified by others.

Can you imagine how different your life would be if your children, life partner, friends, colleagues, managers or employees were self-aware?

"Be the change you want to see in the world"

When experiencing a lack or suffering in life, we tend to fall into a scarcity mindset and blame external factors. We want to change the world, yet it is up to each of us to choose to perceive and form our own reality and what daily decisions we take, leading us to success or misery.

A consciously cultivated self-awareness enables us to strive purposefully for a more compelling vision, something that motivates and makes us more agile on the way.

The real transformation starts from learning to objectively question our beliefs and to form our visions.

Building self-awareness leads to having clarity on who we are, what or who belongs in our life, and what we truly want to achieve in all dimensions of our being, as opposed to what is expected of us by our environment. It's about navigating through life in a way that's aligned with our core, so that we don't have regrets at the end of it.

It's key to understand that unless we consciously build our own roadmap for life, we will not be fully aware of our potential and will fall into other people's agendas, which often lead us away from our true self-actualisation.

My mission

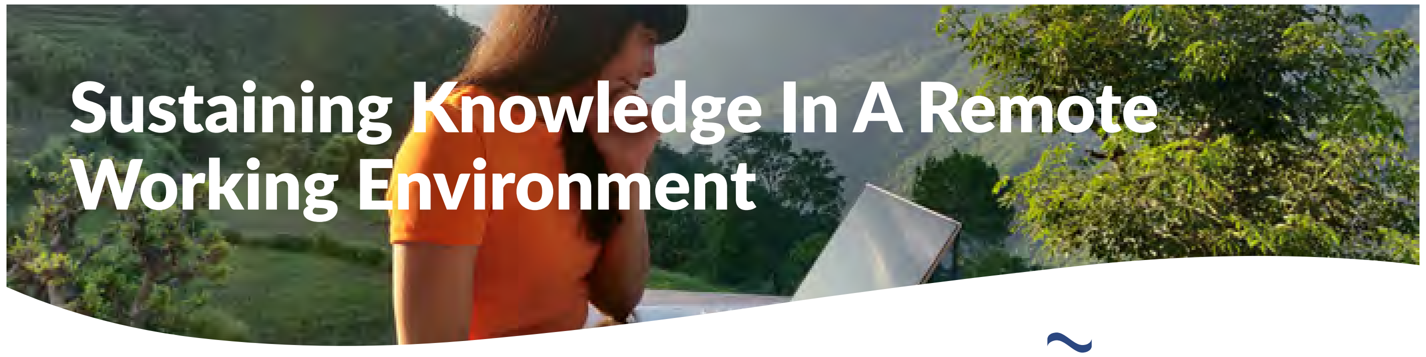
I am now dedicated to support individuals in consciously building their self-awareness and empowerment to reach their true potential, without compromising any area of life.

For more information on my life-transformational programme, visit **www.TheConsciousZone.com** and get in touch.

Anna Lewczuk

Conscious Living and Executive Coach | Holistic Health Practitioner | Certified Lifebook Leader

THE CONSCIOUS ZONE



Sustaining Knowledge In A Remote Working Environment

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Data democratisation – the school of thought that data should be made readily available in an organisation rather than being kept in silos – is a concept that is only just emerging in Retail Banking. It has, however, been a consistent theme in our thought leadership articles. It should resonate with all aspects of the Financial Services Industry.

With the correct controls in place, specifically making data available to the right people at the right time, the concept is very powerful. Sustaining and sharing knowledge is critical for day-to-day operations, as well as providing sufficient audit trail for legal, compliance and external auditors. Accrued knowledge should aid better decision-making.

But sustaining knowledge assumes that the knowledge is available in the first place and this has been a critical component in remote working over the last 18 months. Remote working is here to stay, so the better provisioned we all are, the better.

Preserving secure, controlled access to that data is as big a consideration as what the data is and does: front and centre of any decision to adopt new technology must be complete security of that data. Once that has been assured, then the focus can turn to scrubbing and maintenance, essentially data integrity. Doing this is a truly integrated system has very obvious benefits, too.

A 2018 survey by Experian had Banking Industry respondents suggested that – on average – as much as 30% of their data was inaccurate. So having confirmed how safe the data is, the next task should arguably be checking for accuracy and veracity of that data. At which point sustainability and sharing of the clean data can become a reality.

The benefits are obvious: we have acknowledged that better informed decision-making would be one, and innovation would be another, on the basis that a better empirical starting point will underpin further exploration and extension with far greater confidence.

Furthermore, McKinsey research reveals that in 53% of cases, teams requesting access to internal data beyond their departmental remit, the response time could be measured in months. Shorter response times, error reduction and the consequent re-focussing of resource are all material operational benefits which – in an integrated solution – can all be tracked and measured.

If the benefits of a fully accessible centralised data store are obvious, then understanding how this fits with wider considerations is just as important: ISSA's recent Working Group report on Operational Resilience highlights APIs, automation and the Public Cloud as specific technology capabilities. Importantly, people and processes must be intimately involved in resilience and sustainability, not least when we layer in geography.

London to Hertfordshire is the same as New York to Mumbai or Melbourne, and Paris to Buenos Aires: if the platform fits the bill and it is both practical and cost-effective - and it overcomes the challenges of in-house builds, not least in these straitened times – then such a platform merits further enquiry.

Simon Shepherd

CEO,
MYRIAD Group Technologies Limited

myriad Group Technologies Ltd

Accelerated Settlement – The Move Towards T+0

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Despite the ongoing global transition towards a harmonised T+2 settlement cycle, a number of market participants believe improvements are still needed. Following the unprecedented market volatility in 2020 and 2021, there are growing calls in certain quarters for a further compression of the existing T+2 settlement cycle to either T+1 or T+0. However, such a shift will not be a straightforward exercise.

Amid growing scrutiny of the current T+2 model, some within the industry – most notably the Depository Trust & Clearing Corporation (DTCC) – have pushed for the introduction of a T+1 settlement system. T+1, argues the DTCC, will bring about major cost savings, reduce market risk and lower margin requirements. However, a market-wide shift in the US to T+1 is not without its challenges, and these need to be overcome first. Most significantly, a market that chooses to adopt T+1 risks causing huge logistical problems, especially for investors operating across different time zones. This could create massive inefficiencies around trade matching and end of day reconciliations.

A pivot to T+1 would also force FX to be booked on the same day or T+1 meaning all parties in the settlement chain will need to confirm the trades on trade date, something which could create issues around pre-funding. In addition to potentially exacerbating market fragmentation, T+1 could result in increased settlement risk and fails - leading to penalties and mandatory buy-ins under regulations such as the Central Securities Depositories Regulation's Settlement Discipline Regime in the EU.

While there is scepticism about the merits of introducing a T+1 settlement cycle without impacting the value chain, market practitioners are becoming more open to the idea of T+0 or even atomic settlement. Again, the benefits of shorter settlement cycles (e.g. less counterparty risk, capital and liquidity savings) ring true for T+0 just as they do for T+1. Whereas the shift to T+1 is leveraging existing systems, a transition to T+0 would require the industry to embrace new technologies such as DLT [distributed ledger technology], smart contracts and central bank digital currencies [CBDCs].

So how would these technologies usher in T+0? DLT provides a real-time, single source of truth, while smart contracts can be utilised to facilitate securities and cash settlement in what would create an ecosystem supporting atomic settlement, namely the simultaneous transfer of cash and securities. This could help market users procure massive operational and cost savings, especially as instantaneous settlement would remove the need for CCPs.

Similarly, the emergence of central bank digital currencies (CBDCs) could play a role in bringing about T+0. CBDCs – namely digital iterations of fiat currencies issued by central banks, which are stored on a DLT – engineer efficiencies in securities settlement by using central bank money. As investment into these technologies increases, the possibility of delivering on T+0 will grow. However, there are stumbling blocks which need addressing. Today, technologies such as DLT and smart contracts are not subject to uniform industry standards or common regulation. Without some degree of basic harmonisation, the ability for market participants to interoperate with each other in post-trade processes such as trade settlement risks being undermined.

More fundamentally, T+0 will never be achievable unless other activities in the investment value chain become real-time or instant as well. For example, if payment settlement systems and FX processing continues to rely on antiquated or legacy technologies, then T+0 will be harder to achieve. Only unless there is meaningful digitalisation across the entire transactional life-cycle will T+0 become a reality.

For the full article see https://*flow.db.com/securities-services/accelerated-settlement-the-move-towards-t-0*

Mike-A Clarke

Global Head of Product Management Securities Services

Deutsche Bank

Deutsche Bank

Two Decades Is Too Old For A Post-Trade System

GBST's Head of Capital Markets, Denis Orrock, talks to The Network Forum about legacy post-trade systems, what they have in common with flip phones from 2001, and why implementing a modern, cloud-based middle and back-office platform makes sense, just like using a smart phone in 2021 does.

Who remembers the mobile phone they used 20 years ago? It certainly was not a smart phone. It may have been adept at making calls and sending a few over-priced SMS messages, but it was worlds apart from the multi-functional device we have all become accustomed to.

Smart phones are now an indispensable part of life and the form factors of 20 years ago are a distant memory. Integration with cloud services, AI assistance, and today's desktop-quality apps make the use of mobile phones a predictable and seamless experience. In business, similar advances are also evident. Computing speeds have multiplied by 100 and the rate of data transmission has increased by 50. The cloud delivered tectonic changes in software delivery with modern business applications now predominately delivered via a web browser.

In financial services, trading volumes are higher, settlement is faster, and retail investors and institutions all expect fully automated, reliable settlement and asset servicing.

So why are so many banks and custodians still using post-trade systems designed 20 or 30 years ago? And why do banks continue to operate regional or asset class-specific post-trade systems - even while trading, risk, and ERP systems have been modernised and consolidated to provide global, firm-wide coverage?

The answer can be provided in one statement:
Continually increasing complexity.

Continually increasing complexity

Post-trade systems are notoriously complex, connecting to dozens of systems both within and outside of a bank. They are the books of business and records that nobody wants to touch in case they break. They are programmed to deal with grey zones such as market idiosyncrasies, differing settlement regimes, variable messaging standards, data quality issues, and more. Most of these systems were designed when the markets moved to electronic settlement around three decades ago, and while they have been progressively upgraded to cater for market changes, they remain fundamentally on the same technology base.

Compounding the issue, many banks have separate post-trade systems for equities, fixed income, and derivatives, with even more variation on a regional basis. The outcome is strangled business growth due to high operational and change costs, data 'fog', system failure risk, and an inability to take advantage of contemporary technologies such as cloud and AI.

If using your phone and laptop from 2001 in 2021 does not make sense, then using a legacy back-office platform should not either. Implementing a modern cloud-optimised back-office system with the flexibility to cater seamlessly and efficiently to growing market needs and changing regulations is an achievable goal for every firm.

Modern systems should cater to multiple asset classes and operate across numerous markets. Take a system that processes equities and fixed income, for example. Connectivity into different clearing houses and central securities depositaries (CSDs) is required, along with support for each asset class's messaging and regulatory mandates. Compliance or operational restrictions may require the fixed income and equities operations teams to be separate, or the efficiency provided by a single operations team may be preferable. Regardless, a system should cater for either. An extension into middle-office processing or new business lines should also be possible in the same cloud-based system that scales automatically to meet increased usage demand. Post-trade exceptions across any market or asset class should be managed in the same system, with quality of life, business, and regulatory changes updating in real-time, allowing the organisation's users to modify processing rules to cater for these changes.

Change management

Implementing a new system can be challenging and is frequently underestimated. Risk management is key. Commencing with a small market or problem area to ensure a system can grow into adjacent markets or asset classes is sensible and minimises the deployment risk.

A market trigger such as a new clearing house, CSD system, or messaging implementation provides the perfect window to consider system change. The correct system configuration from the outset will help avoid costly modifications down the track. This could include a review of the entities transacting and clearing in each market and the definition of how business activity is fed to downstream systems for accounting and analysis. Once the need for change is identified, the implementation of the new system can be managed by the vendor so that the organisation can focus on ensuring an optimal system foundation is provided for near-term and future usage.

Consider how the system will support business growth in areas such as broking, stock lending, agency flow, and principal book trading. Decide whether it will make sense to include affiliate or external custody services in the same system. Although outside the post-trade environment, the firm's trading system environment is also important to review. If multiple trading systems are used globally, having a stand-alone middle-office allocations engine may ensure continuous flexibility in the trading room, while providing a consolidated, organisation-wide view of trade-day activity.

The proof

Deploying a modern, post-trade system is not unprecedented. GBST's recent Syn~ implementations have enabled clients from disruptive start-ups to tier-1 global investment banks to seamlessly consolidate middle and back-office operations across multiple geographies, entities, and asset classes for improved ROI. So, is it time to upgrade that flip phone?

Denis Orrock
Head of Capital Markets
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GBST | Financial Services Technology

Collaborate To Regulate: How Targeted Engagement Helps Investors Access Emerging Markets

It is easy to underestimate the pace of change in frontier and emerging markets. Barriers to commerce are falling quickly, with many governments in Asia, Africa and the Middle East committed to making life easier for investors, as a means of attracting overseas capital and knowledge. Some even see an opportunity to steal a march on Europe and North America, by embracing smarter regulation and digital finance. Benefits can be seen in markets where local regulators are open to discussions with market participants to help them make this transition.

Lessons from Greater China

When it comes to nimble regulations, frontier and emerging markets can take inspiration from China, Hong Kong and Taiwan, whose regulators realised that when it comes to financial services, success means quickly updating the rules to reflect changing circumstances and technology. This has never been more important than over the past 18 months.

Regulators across Greater China have been open to adapting to the new environment while reducing network risk. In Taiwan, for instance, foreign institutional investors seeking to open a brokerage account must submit physical paperwork in order to do so – something made much more difficult by social-distancing and remote-working during the pandemic.

Financial institutions, including Standard Chartered, have been working with the Taiwan Depository & Clearing Corporation to find a system that is more resilient to this kind of disruption. The result is the eSMART system, which will allow securities dealers to digitally handle, transfer, and maintain various book-entry transfer documents via the new platform. It is hoped that the platform[1] will launch before the end of this year.

Regulators in the region are amenable to easing such pain-points, but first they must know where they are. In China, for instance, until recently there were two different regulatory and quota regimes for Qualified Foreign Institutional Investors (QFII) and for RMB Qualified Foreign Institutional Investors (RQFII).

This system complicated the repatriation of profits, hindered trading and created a burdensome amount of documentation. Financial institutions made representations to regulators such as the People's Bank of China, China Securities Regulatory Commission and the State Administration of Foreign Exchange in order to explain how the system could be streamlined to encourage more activity.

China's regulators listened. In June last year, they published new QFII/RQFII rules to simplify market access and expand the scope for investment

Helping higher-barrier markets improve access

Other frontier and emerging markets are realising that they can attract greater local investment by working with market participants to create smarter regulations. Take Kenya. There, recent governments have devoted time and energy to improving the business environment, and the results are paying off – the East African nation now ranks above countries such as Italy and Chile in the World Bank's widely watched Doing Business ratings.[2] This spirit of reform has extended to financial services, including when it comes to open conversation.

A law in 2019, for example, reduced the threshold of shares that a bidder would need to acquire a company from 90% to 50%. With just half the equity, the new owner would be able to buy-out the minority shareholders on a mandatory basis and then de-list the company from the Nairobi Stock Exchange.

Given that the Doing Business index includes the protection of minority shareholders as one of its key metrics, having such a low threshold was likely to have a negative effect on Kenya's ranking, which Kenya's national assembly is keen to improve still further.[3] Leading Kenyan and international banks, including Standard Chartered, lobbied the government to revise the legislation, and in February 2020 the 90% threshold was restored.[4]

Sharing experience through engagement

By sharing what we've learnt from working not only in their domestic markets but in many others, market participants can engage regulators on the developments and changes that would drive greater market participation.

This collaborative approach also allows us to help our own clients reduce their risks from operating in such markets. That in turn makes frontier and emerging markets more attractive to investors, expediting their national growth and strengthening their resilience to external shocks.

Standard Chartered

1. *https://www.tdcc.com.tw/portal/en/news/content/40289795770573000177f-10b412f0060*
2. *https://www.doingbusiness.org/en/rankings*
3. *https://www.the-star.co.ke/business/kenya/2020-01-17-change-takeover-law-to-protect-minority-shareholders--adan/*
4. *https://www.businessdailyafrica.com/bd/corporate/companies/state-revises-firms-hostile-buyout-law-2279882*

Ode to TNF

By Rupert Booth

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In the interest of business and matters financial
Some fairly lightweight, others substantial
The Network Forum gave us space to hold forth,
From all round the Globe, East, West, South and North,
On subjects that concern the great houses of commerce
And other material discussed in this verse.

Kicked off, as usual, with humour and japes –
Banking professionals threw soccer skill shapes –
And Theodora flew into Rachel Bo's arms…
A pure piece of theatre; oh how we were charmed!
Starting the show with a warm cosy glow,
And got us all going, as per the below:

All over the platform, from Stage to Expo
Sang custody, clearing, regs and crypto
An agenda spilled over with slick virtual action,
To stimulate insight and strong interaction.

Mr Cameron regaled us from the BNP booth
With insight on AFME, so urbane and smooth,
As the panels all fizzed with sound revelations
Operational insights from so many nations,
Shedding sage wisdom on operational resilience
Delegates demonstrating knowledge and brilliance.

I have to be honest, a highlight – unplanned –
At the end of day one, when wine was in hand,
Took place far away from our august assembly,
As two goals were scored by England at Wembley*
The English have decided they'll now win the lot
Not so fast – don't forget the penalty spot!

Enough of the sport since we're all here for work,
But laced with some fun – there's always a perk,
It has to be said, as we close and reflect
On a splendid event, Team TNF - respect!

And once we're back together next year,
We'll raise all our glasses together and cheer,
On the beach, one hopes, at the end of a day…
Of shaking hands in the old-fashioned way.

**Apologies to Germany.*

THE NETWORK FORUM

The Digitization Of Capital Markets

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Technology and trusted data are critical to success in an increasingly interconnected global economy–yet the software systems underlying services and commerce are isolated, disconnected, and inefficient. Poor or nonexistent communication between core business systems leaves customers, partners and vendors without shared, authoritative data. As a result, interactions are anything but seamless: each party must constantly reconcile records, introducing risk and embedding unnecessary operating costs.

With many institutions dependent on aging technology, rigid architecture, and information silos, meeting today's customer demands and addressing regulatory requirements is hard enough; innovating for tomorrow may seem insurmountable.

For capital markets, these challenges ring true. Digital transformation initiatives are speeding up the pace of business. Yet asset-based transactions continue to run on slow, sequential settlement processes fraught with high costs and risks. Today, every player across the post-trade process is required to check and enrich data about the trade, matching and reconciling it with their counterparties before instructing the next participant in the chain. Most interactions between firms are executed using bilateral, message based communications, which lacks transparency and reliability.

The sequential settlement process also has high transaction costs. Despite these costs, there's little transparency. Without visibility, there's no certainty on the finality of the settlement. The purchasing party doesn't know the transaction status until after they've acted. The delivering party may have met the contract obligations; they may not have.

Driving a digital future for capital markets

We see unprecedented growth and innovation across the systems and market infrastructure powering our global economy. In a recent Nasdaq study commissioned from Celent, CIO Market Infrastructure Survey 2021: The Digital Journey to 2025, capital markets were ranked as one of the top industries preparing for massive changes in the next few years.

Predicting a 45% increase in the number of the Market Infrastructure (MI) providers with fully modernized technology stacks by 2025, Celent states that, "a combination of drivers, including regulatory, market forces, emerging digital models, and lately, the pandemic response, are contributing to a shift in the technology and data demands of market infrastructure."

As market infrastructure evolves to support new digital models and asset classes, many firms are moving forward with POCs that validate investments in digital transformation initiatives to improve how exchanges, clearinghouses, and custodians operate across the holding chain.

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Bursa Malaysia and Deutsche Börse are two recent examples of such initiatives.

In September, Bursa Malaysia Berhad ("Bursa Malaysia" or the "Exchange") announced plans to embark on a Dematerialization Proof-of-Concept to facilitate the dematerialization of securities certificates leveraging Daml smart contracts from Digital Asset and a highly scalable distributed ledger platform from VMware. The project aims to test blockchain-powered technologies' efficiency and operational feasibility in the issuance of dematerialized securities certificates, with initial emphasis on Structured Warrants.

The blockchain-powered proof-of-concept will aid in the simplification of Structured Warrants issuances. It provides a centralized source of truth to increase transparency, improve data quality, and reduce potential disruptions in physical transportation and in-person delivery throughout the eligibility life cycle. In addition, the proof-of-concept employs electronic vaulting technology for data storage and transportation, and an e-signature method for digital certificates execution, resulting in improved Structured Warrants eligibility and issuance processing.

Bursa Malaysia estimates this initiative could improve the ease of doing business by reducing the reliance on manual work to create, manage and withdraw Structured Warrant certificates.

In October, global market infrastructure provider Deutsche Börse unveiled plans to launch a regulatory compliant, fully digital post-trade platform called D7, anchored in the recently introduced German digital securities law framework. The new cloud-backed and DLT-ready D7 platform will enable market participants to digitize their financial products with continuing access to both existing central and distributed infrastructures and markets.

The D7 platform is being developed jointly with a dedicated market community and with long-term strategic technology partners, such as Digital Asset. In the first phase of the project roll-out, Deutsche Börse is working with Digital Asset to build a central registry system. For the first time in Germany, the new registry, built on a centralized database and other tools form the basis for issuance and custody of dematerialized securities in compliance with new legislation introduced earlier this year.

D7 will also support same-day-issuance and paperless, automated straight-through processing for certificates and warrants issued at Clearstream Banking AG. To this end, Deutsche Börse will leverage Daml smart contracts from Digital Asset to create and process Digital Instruments, the digital description of (electronic) securities, to manage the securities alongside the entire value chain.

A market ripe for innovation

It's an exciting time for capital markets. Dematerialization of securities and digitization of issuance processes is at the forefront of change in capital markets. A digital future for capital markets will not only enable interoperability between financial institutions but bring greater levels of efficiency, security and transparency to market participants worldwide.

Digital Asset