



SPONSORED SECTION

EVOLUTION IN THE COLLATERAL MANAGEMENT SPACE

OVERHAUL IN THE MARKET

The impact of the 2008 financial crisis continues to be felt throughout financial markets around the world. Globally, regulators have responded quickly, drafting a series of proposed reforms that are intended to reduce systemic risk by providing greater transparency and increasing the amount of risk-weighted capital that firms are required to hold. The list of new regulations is lengthy; the 2,300-plus page Dodd-Frank Act, tri-party repo infrastructure reform, Basel III, Solvency II, Markets in Financial Instruments Directive II (MiFID), European Market Infrastructure Reform (EMIR), to name a few. Many will have meaningful impact across global markets; the ultimate goal is that financial institutions are better able to withstand volatile markets and unexpected shocks to the system. A key focus of much of the new regulations revolves around the importance of a robust market infrastructure through which an ever-increasing amount of securities and derivatives trading and settlement is expected to occur. Accordingly, business models are changing, and traditional practices in the repo, securities lending and derivatives markets are evolving. Broker-dealers, banks, institutional investors and other market participants are adjusting their organizations and their strategies to succeed in a more highly regulated environment.

EVOLUTION OF COLLATERAL FINANCING

The crisis of 2008 brought to light the interconnectivity amongst the larger financial institutions and the inherent risks that this brings to global markets. The downstream impact that institutions have on the broader financial markets and the overall economy during periods of extreme stress became abundantly clear. In response to the new regulations and the challenges of the prevailing economic environment, market participants are facing new challenges in obtaining funding, managing counterparty credit risk and securing appropriate collateral. In this new environment, market participants are looking to service providers to offer innovative technology solutions to improve operational efficiencies.

“To keep up with all the changing trends and needs, we have to work more closely with clients, regulators and the industry as a whole to develop innovative solutions that help reduce risk in the collateral management space,” says John Vinci, head of Global Product Management for BNY Mellon Broker-Dealer Services.

Additionally, these challenges have sparked an evolution for collateral financing. Some current collateral financing transaction trends include:

Longer Durations

Globally, in the repo market, the trend is moving toward longer durations for term financing. While historically overnight financing was most common, longer-term financing allows for dealers to more effectively manage their liquidity needs.

Account Segregation

Investors are looking for segregated accounts to safekeep margin payments so that margin is fully segregated from their counterparty's proprietary book in the event of a default.

Move to Central Clearing

Globally, regulators are seeking to change how over-the-counter derivatives markets work by suggesting the involvement of central counterparties or utilization of exchange-traded models in transactions.

BENEFITS OF COLLATERAL MANAGEMENT:

- Transparency
- Valuation of Collateral
- Collateral Screening and Eligibility
- Collateral Optimization
- Operational Efficiency
- Mitigate Counterparty Credit Risk





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John Vinci

HOW BNY MELLON CAN HELP:

- Financial Strength
- Comprehensive Collateral Management Services
- Strong Capital Position
- Integrated Technology
- Experience and Expertise
- Global Presence

The new regulations and trends are affecting nearly all large financial market participants in one way or another, and more so those institutions active in the repo, securities lending and derivatives markets. While the impact of some of the new regulations has become well understood, many open questions remain. Moreover, some of the new reforms, such as Basel III, will be implemented in phases requiring entities to address, adopt and conform over time. BNY Mellon is committed to maintaining active dialogue with key regulators, multiple industry bodies and our clients to stay at the forefront as change unfolds. This will help prepare us in leveraging the breadth of our firm-wide capabilities to help clients meet their business goals in the new environment.

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Increasing Need for Quality Collateral

Perhaps one of the most significant trends taking place is the demand for higher-quality collateral. Market participants are holding on to “flight to quality” collateral instruments, as they are the most liquid, non-cash collateral. Yet, with global markets moving toward central clearing, there is a greater need for the use of the same high-quality collateral for posting to exchanges. The potential shortage of high-quality collateral highlights a need for greater optimization so valuable collateral is used most efficiently.



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