



## Depth and breadth: the Nordics do it properly

Nordic beneficial owners tend to be more conservative, but only because of the level of due diligence they conduct and the depth of understanding they want to have, says Stephen Kiely of BNY Mellon. Mark Dugdale reports

### How would you describe securities lending in the Nordics?

Securities lending in the Nordics is not different from everywhere else, particularly continental Europe, but there are some nuances. Nordic beneficial owners tend to be more conservative, but only because of the level of due diligence they conduct and the depth of understanding they want to have. This is often greater than beneficial owners in other countries.

Once they know the finer details, Nordic beneficial owners are often both happy to get involved in securities lending and publicise the fact. The Nordics is a region where due diligence has a high priority, not only when it comes to organisations, but also for both processes and procedures. Nordic markets have historically enjoyed steady growth in securities lending, and it's showing no sign of slowing down. They are textbook markets in that respect. We are seeing beneficial owners that have lent previously come back in as well as new lenders entering the market.

### What are the beneficial owners doing business in the Nordics?

We're in a climate where the lines between pension fund, asset manager and mutual fund are being blurred all the time, so anyone trying to earn incremental revenue from long inventory is either looking at lending, or already in the market. Having

said that, we're seeing the equity index managers specifically looking at lending and coming into the market in order to try to get some pick up in the yield, especially those that have been set benchmarks. It's not always about the money, it's about beating the benchmark.

In fact, I'd go as far as to say that we're seeing greater interest from participants that are holding assets that are pre-prescribed, whether it's index tracking, or whether they just have to hold a certain percentage in AA government bonds, and so on. Wherever there is a pre-prescribed investment management remit, we're seeing an interest in lending in order to get across that benchmark.

### What are the most attractive trades?

The first half of 2015 has been about the oil companies. It began at the end of 2014 and continued through Q1 and Q2 2015. There were six to eight oil companies, especially in Norway, which, due to downward pressure on the price of oil, attracted the attention of short sellers, making them more sought-after in the lending market. In terms of Nordic assets, there have been specials outside of oil, but in the general collateral names, it's been business as usual.

Additionally, seasonal activity in Europe has driven revenues and we're seeing some pick up on fixed income lending. However, this tends to be only where

the lenders are accepting equities as collateral and they are willing to perform the upgrade trade.

## Will collateral upgrade trades become more prevalent in the future?

I think so, and there are two drivers that will likely determine whether or not this happens. The first is expanded collateral parameters, specifically in terms of the indices that are accepted.

Also, I think we'll get to a stage where physical exchange-traded funds (ETFs) are accepted as collateral. Secondly, I think that the advent of central counterparties (CCPs) for securities lending will see participants relax their collateral parameters to a certain extent.

## Which regulations are you seeing hit the Nordic markets?

The liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) are affecting the Nordics and wider Europe. They are changing the dynamics around high quality liquid assets (HQLA) and are forcing participants to look at their balance sheets and consider what they need to keep or remove in order to aid efficiency and optimisation. This is driving both the supply and demand sides of securities lending at the moment.

The LCR and NSFR have also caused a pick up in government bond activity. In terms of needing HQLA, Nordic government bonds are very attractive as collateral but they are not as common as US treasuries, for example.

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## What about ETFs as collateral, given that Nordic bonds might be few and far between?

Right now, ETFs as collateral is not common, but there is a lot of noise about them from the main players in the ETF market, who, understandably, are very interested in increasing their liquidity. We are also seeing queries on ETFs as collateral from one or two of our advanced clients. They are asking the question internally, "if they can accept a basket of collateral, why can't they take packaged collateral in the form of a physical ETF?" In times of stress, this is arguably more liquid.

However, this concept needs to be socialised as an idea before it becomes the norm. It is worth noting that beneficial owners in the Nordics have historically not been the first movers when it comes to these changes in behaviour.

## What about the future?

Interest in CCPs is growing faster than ever. There's a general acceptance that CCPs will be an 'as well as' rather than an 'instead of' addition to the demand side of securities lending. Now that we're seeing borrowers start to push the CCP model more, due to balance sheet constraints and netting considerations, I think we will see changes in pricing if the ability to trade through a CCP exists. The first clients into the CCP trade will be those who already have experience in trading derivatives, as they are comfortable with the central clearing model. [SLT](#)

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