Entering a new era

ISLA's CEO Andrew Dyson and first female chair Ina Budh-Raja speak with Carmella Haswell on the Association's three-year strategy as the industry undergoes an unprecedented period of transformative change

The International Securities Lending Association (ISLA) is paving out its next steps in leading the industry through periods of transformation, with a new board of directors and its first female chair and person of Asian heritage taking the reins.

"It is an exciting time to be taking on the position of chair as the industry undergoes an unprecedented period of transformative change," says ISLA chair Ina Budh-Raja. The ISLA team and previous board of directors, which Budh-Raja has been a part of for the past three years, have built the foundations essential to supporting members through the forthcoming evolution of the securities finance industry.

The post-financial crisis regulatory reform agenda is now well-matured and a new era of regulatory policy is taking shape, Budh-Raja notes. The board is ready to address future priorities such as digitisation, sustainability, increased investor and consumer protection, with an overarching focus on market efficiency, resilience and accountability.

Entering a new era for the Association, a revised three-year strategy, extending through to 2025, gives detailed attention to the digital agenda, which covers the tokenisation of conventional asset classes, as well as the introduction of new 'native' digital assets.

In November 2022, ISLA released a report proposing alterations to the Global Master Securities Lending Agreement (GMSLA) to allow for market engagement with digital assets. The paper, entitled 'Preparing the Global Master Securities Lending Agreement (GMSLA) for an Evolving Digital Asset Landscape', discussed how digital assets could transform liquidity management and revolutionise the global securities finance industry. It further pinpointed elements within and outside of ISLA's remit that need to be addressed, including legal, commercial and documentation issues.

"There is no doubt that new and novel asset classes, including digital and crypto assets, are increasingly demanding the attention of the investment community," notes ISLA CEO Andrew Dyson. "As these asset classes come into the mainstream, it will be important for those that serve these industries, including securities lending, to be duly prepared to support them."

The report highlighted the message that digital assets would revolutionise the market. For Dyson, the paper presents a fundamental first step in analysing the key considerations and potential issues that may arise when incorporating digital assets, and sets out a long term agenda for their discussion and resolution.

As markets begin to embrace these new asset classes, preparations will continue on the digital agenda. Dyson states that the Association's work on the Common Domain Model (CDM) will provide the foundation for much of this development. "I would also expect to see more from the joint associations (ISLA, ICMA and ISDA) as we build out our respective data models, with the move to a true open source environment through FINOS being transformational," he adds.

The global sustainable policy agenda will also become a dominant theme for ISLA. It is an agenda that impacts all corners of the financial markets and requires the industry to adapt to consider environmental, social and governance (ESG) factors and to maintain liquidity in the capital markets. Continued market education and advocacy will be required to prevent attrition of lendable assets, says Budh-Raja, to maintain stability and liquidity underpinning the broader markets.

ISLA will also assist members in navigating the regulatory frameworks that are developing around digitisation and sustainability. This will require further analysis and advocacy to drive robust, risk-managed and, where possible, standardised outcomes for the industry.

In line with ISLA's geographical remit, the Association is deepening its coverage of the Middle East region, recognising that these jurisdictions are now rapidly developing their capital markets infrastructure and that securities lending is a priority in the region as a foundation for deep and liquid markets.

As part of ISLA's aforementioned three-year strategy, 2023 will see continued engagement and advocacy with policy makers in the region, development of market structure guidance, standardised legal documentation wherever possible — including entity-specific considerations such as Sharia constructs and revisiting netting capabilities in relevant jurisdictions. Budh-Raja adds: "While this is a sizable book of work for the ISLA team, it is one which will support new opportunities for members operating both in the region and on a cross-border basis."

Accounting for D, E and I

By taking on the position of ISLA chair, Budh-Raja became the Association's first female lead since it was formed 35 years ago. "In my 25 plus years of working in financial services, I have learned from personal experience that representation really matters. At a very basic level, it is important to see 'people like you' performing well in roles which may otherwise have seemed inaccessible within historic systemic norms."

Budh-Raja remains an active advocate for diversity, equity and inclusion (DEI), having worked alongside the Women in Securities Finance organisation for the past five years as co-lead of the London chapter.

"I have certainly been inspired by examples of positive representation and it is therefore incumbent on me — and others like me — to step into leadership roles where possible, even if that means facing our natural fears of being 'the first (female)' in the position," she adds.

Not only does Budh-Raja hold the metaphorical torch as the first female ISLA chair, but she also represents the first ISLA chair of Asian heritage, an achievement that is equally important for Budh-Raja in terms of embedding DEI in the industry and creating a level playing field for people from all backgrounds, across several diversity factors.

"Diversity of skill sets and perspectives is essential to the growth of our industry," Budh-Raja explains. "I hope I can serve as an example, at least in some small way, to others who work in securities finance roles which may traditionally have been viewed as tangential to the business, but in fact, are increasingly critical components of a well-functioning, progressive business."

DEI will form an intentional strand of the overall ISLA strategy going forward. By the end of Q1 2023, new policies and procedures will be in place to embed DEI criteria more formally, including the creation of a Code of Conduct, now in place, to cover ISLA events and policies outlining DEI considerations for the events team. A series of DEI initiatives is soon to be announced by the organisation.

Dyson concludes: "As an Association that seeks to include all in the work that we do, I firmly believe that we have a very real responsibility to pursue diversity, equity and inclusion across our industry into all facets of our lives. ISLA has a real opportunity to drive the reforms needed to deliver a diverse and more inclusive workplace environment and helping to deliver on those objectives will be an important part of our collective efforts this year."

An important year ahead

Systemic risk events have tested the financial markets to the extreme, says Dyson. Considerable volatility put pressure on the markets, and the banking sector more broadly, during early 2022. Following the UK mini budget in autumn of 2022, market participants also faced intense volatility in the UK Gilt market, which led to the so-called liability-driven investment (LDI) crisis — leaving market participants struggling to fulfil margin obligations under long-term swap transactions.

Although order was restored after the intervention of the Bank of England, Dyson warns that the industry needs to be mindful of the messages that these events have sent, as the market continues to think about liquidity and, notably, the availability of collateral.

The impact of the sudden and dramatic demise of FTX in 2022 has added to this market uncertainty. "Many of the issues swirling around the company and its founder relate to very familiar themes associated with proper and transparent governance and oversight," Dyson indicates. "Some of the work that we are looking to do at ISLA around documentation for that segment of the market will be part of an inevitable process as this market evolves and matures."

Evaluating the financial landscape, Dyson believes 2023 will be an important year for the industry. Opportunities are arising with risk-weighted assets (RWAs) and total return swaps (TRS) front and centre, while the regulatory agenda is set to alter as new narratives emerge.

In his analysis, Dyson says: "As the real impacts of the implementation of the Basel framework become clear, we are already seeing the market actively looking at new and different ways of transacting business that either negate or significantly reduce RWA charges associated with the traditional lending model."

Market participants are paying increasing attention to pledge collateral

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Chair
ISLA

models, with Dyson anticipating an acceleration in their use, especially if so-called regulatory uncertainties around the structures are resolved. In addition, synthetic lending in the form of TRS are attracting a considerable focus from the market, due to the lower RWA costs associated with derivatives, as well as the ability to net street and client trades from a balance sheet perspective. Dyson predicts that the use of TRS will grow exponentially throughout 2023 and 2024 as lending agents look to develop greater capabilities in this area.

The reduced number of brokers in the European market today is impacting market behaviour, notes Dyson. He explains: “While it is acknowledged that the remaining incumbents have taken up much of the flows from departing firms, the market is now, in my view, struggling with single counterparty concentration issues and therefore looking at other ways to get securities to the end users.”

A direct implication is that central clearing — that has for long been problematic for the market — may now be welcomed more widely as a solution that diversifies risk and reduces RWA costs.

Budh-Raja states: “We are at an inflection point, where market participants are having to adapt at pace to solve for new regulatory changes, resource constraints and to manage capital more acutely to remain competitive.” The combined effects of changes to the Basel framework, RWA implications and single counterparty concentration limits require firms to be nimble, resource efficient and to have a suite of solutions available to them, Budh-Raja adds, which may include increased use of pledge collateral arrangements, the emergence of agency synthetic TRS solutions and a new advent of CCP solutions.

EU and UK markets are to face tremendous regulatory change in 2023 as policy makers address factors highlighted by recent market volatility, as well as tackling the systemic and cultural changes necessitated by digital transformation and sustainability agendas.

Budh-Raja continues: “We are already seeing the beginnings of policy divergence in a post-Brexit world and the impact on the financial services' regulatory agenda is increasingly complex as we adapt to parallel regulatory regimes, while operating global businesses straddling nuanced regulatory differences.”

The ISLA chair expects to see significant regulatory and policy developments associated with the broad sustainability and digital agenda, as well as investor protection and fund structure regulation — which will all require strategic advocacy and active representation from a securities finance perspective.

As an association that has its membership now largely split between the EU and the UK, Dyson notes that it is important that ISLA works actively with its respective member firms to ensure that the Association continues to deliver the right outcomes as these two areas potentially diverge.

Budh-Raja concludes: “It is imperative that ISLA is one step ahead in supporting its members through this period of change and innovation, advocating with regulators for pragmatic outcomes which are compatible with securities lending and do not result in inadvertent limitations on this market.”

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