Adapting to a changing securities finance environment

By consolidating securities finance, collateral operations, post-trade processing and risk management into a single system, clients can break silos and mitigate risk, says Murex's Sabine Farhat. Carmella Haswell reports

Sabine, having been a part of Murex for the past 15 years, how have you seen the business transform and evolve over this time?

Securities finance is an ever-evolving activity. It has always been the backbone of the financial market — the energy that makes the machine function. In a sense, securities finance ensures shorts are covered, risk is hedged, liquidity is available to fund activity and collateral is available to support and cover activity exposure.

Securities finance players have a key role in executing liquidity mandates and optimising balance sheets. At the same time, they ensure compliance with an increasingly regulated market. We have always been a one-stop shop when there is a need for securities management, as well as liquidity mining. Juggling those mandates comes at a cost. Desks operate complex operations ranging from negotiation, pricing and trading to risk management, corporate actions execution, settlement and more.

Ideally, they should operate on a cross-function, low-touch system to lift the burden of manual intervention and ease communication between desks. What I can see from this perspective is not so much a change, but waves of moving from one product to another and from one mandate to another based on liquidity cost, collateral scarcity and regulations. The real transformation and evolution of the market is seen in the mandatory use of technology to cope with the current era of standardisation, regulation and steps to reduce the total cost of ownership (TCO).

Our users can utilise MX.3 to assist them with the emergence of new products and the shift of mandates. With our cross-asset system, we provide a fit-to-purpose solution and low-touch usage for front-to-back-to-risk-to-collateral across equities and fixed income, while ensuring quick time to market.

What key lessons have you learnt from your time in the securities finance and lending industry and how are you applying these to provide for your clients?

Even though operations, regulatory reporting and risk management can be standardised and optimally be packaged in an out-of-the box system, the financing tools, the optimisation algorithms, position sweeping between desks and cost allocation is very specific to the strategy of the financial institution and its trading decisions. As a result, from a system perspective, it is mandatory to have optimal workflow for operations with the highest straight-through processing (STP) rate, providing credit risk, compliance and a sharp eye on regulations. Flexible and large financing tools that cope with any strategic trading decision and openness to apply the rules and cost of positions and liquidity usage are the way forward.

As a result, in securities finance it is extremely important to understand not just the securities finance industry and the customer, but also what is happening in equity cash, fixed income, liquidity and collateral management. When we see trends in volatilities for equities or new indices in the market, we know that in a few months it will have a direct impact on securities finance, because we are financing the inventory of equities and fixed income or raising secured funding. If we want to be ahead of the market, service our clients to the best of our abilities, and provide them with the technology solutions to be able to operate, we need to look beyond the direct industry and monitor widely.

Even though the market operates differently when there is a split between repo, delta 1 and securities lending, equity and fixed income, sell-side and buy-side, in-house, agency or broker, they are always interlinked. Consequently, from a software house perspective, we ensure functionalities are available on all types of securities financing transactions (SFTs), regardless of underlying, desk or actor. This has helped Murex clients that merge desks to have a fully operating centralised desk with a single system.

Lastly, regulation is key in these times. Whenever there is a study or a project on regulation, we need to make sure that we are participating in the workshops and listening to different audiences, because when a project is finalised, it will be too late to develop. We are a software company at the end of the day — we are here to help our clients operate. If we want them to operate correctly, we need to be involved in every step of the regulation.

What are Murex's prime focus points for H2 2023 and going into 2024?

We maintain a focus centred on the three pillars of our offering.

Product catalogue. We want to provide the widest financing tools offering with a full support of all types of underlying, while having a tailored user experience to each product lifecycle. For instance, we recently added total return futures to our catalogue, working hand in hand with Eurex, and the total return swap on iBoxx. We are currently adding margin lending, as we believe this will be the new financing product in Europe with regards to the Eurosystem Collateral Management System (ECMS).

Centralised firmwide inventory and liquidity ladder. Murex is adding the necessary tools to optimise its securities inventory and has added the capacity to algorithmically allocate the best securities for repo funding and collateral allocations automatically. Moreover, we continuously enrich our internal funding module to sweep positions and their cost or gain between desks in a low-touch way.

Automation and connectivity. Securities finance operates in a large system in the market. We need to be connected easily to all service providers and automate our internal processing in a seamless manner — a key area to reduce implementation costs.

Where are you focusing your resources to enhance your MX.3 offering?

In addition to the points above, we have a dedicated group that monitors regulations and their impact on our value proposition, as well as enriching our out-of-box proposal for credit risk management. T+1 proposals from the US Securities and Exchange Commission (SEC), ECMS and Basel are the current areas of focus.

Ultimately, our trademark is our rich product catalogue, which can be booked, priced, monitored, operated and optimised within the same system, front-to-back-to-risk-to-collateral. This is our DNA — everything evolves from this point.

Murex recently partnered with Rabobank to expand its securities finance solution. In what direction will this collaboration take the firm and its clients? Are there plans in the pipeline to further expand MX.3 for Securities Finance?

It was an amazing opportunity to work with Rabobank — I am very proud of this work. It was quite rewarding and resulted in fast-paced time to market. We have adopted this approach in all of our investments. We collaborated with different clients to publish automation of the equity total return swap process and optimisation of securities allocation on money fill repos.

We have published our newly refurbished lending solution, which uses our existing repo and synthetics products. We are continuing to invest in that area to enrich our optimisation offering. Securities finance and collateral management are a major focus of Murex — we aim to ensure that we continuously evolve in these areas.

The richness of our offering comes from the fact that we have clients across regions, and each one brings their knowledge on the same module, which makes it possible to transpose in case of expansion or market availability.

How is technology disrupting the securities finance industry and how is this changing how Murex is engaging with the market?

I don't see technology as disrupting securities finance — I see it more as enabling securities finance. What we can do today, we couldn't have done historically without the use of technology. Technology has provided automation and scaling, the capacity to collect, clean, transform and analyse data for more knowledgeable decisions, accurate pricing, known risk and compliance with regulations, and has provided a major reduction in desk operation costs.

Clients using technology for securities finance today can expand volumes, which should lead to reduced costs and increased profits. This has been a major enabler to the market. The addition of new technology is not disruptive, it is an enablement.

We are achieving major enhancement in securities settlement failures through a highly automated process, for example the algorithmic optimisation of automatic sweeping position cost, accounts and more.

A real, disruptive shift will be seen in the securities finance market when it increases its use of machine learning and artificial intelligence. The disruptiveness will not be operational, but it will come. Will some counterparts be forced out or forced in? Will optimisation be different? Will pricing be different? It will be a new era for the financial market, not just securities finance.

In terms of regulation, where are you seeing the most impact on your side of the market over the next 12 months?

We should no longer say regulation is impactful. It is part of the normal day-to-day business, the quotidian. We should expect to have more regulation, which is more extreme and more real time. As a technology provider, we need to make sure that we have the richest data possible in our system to ensure that, whenever a regulation comes into force, our clients have the capacity to generate the necessary data and report on time with the highest STP rate and with the lowest failure rate possible. When it comes to standards, we need to ensure that we are aware and that we can easily comply by having appropriate API, flexibility and openness.

There are numerous regulations and standards coming into force — the T+1 settlement, Basel III Endgame adjustments, ECMS collateral settlement and liquidity in European central banks, as well as the SEC regulatory reporting for the US. Each has a different impact on the market, vendors must operate to be compliant and support the service on time.

The impact of these new standards and regulations mostly falls on the cost of funding, use of funding and settlement. As a result, for us, it is imperative to be able to accurately monitor the P&L of investments and funding, allocation of internal cost, rating aggregation and calculation to accurately estimate capital charges, settlement situation and accurate generation of instructions, among other factors. All of this impacts our areas of focus for development. We continuously monitor new market standards, requirements and regulation to ensure we are providing our clients with the best service.