



Issues for Depositories Managing Risk in the Post Crisis Environment



March 2010





Agenda

- I. TM Depository Risk Definitions
- II. Risk Comparisons: ACSDA vs Rest of the World with Key Issues



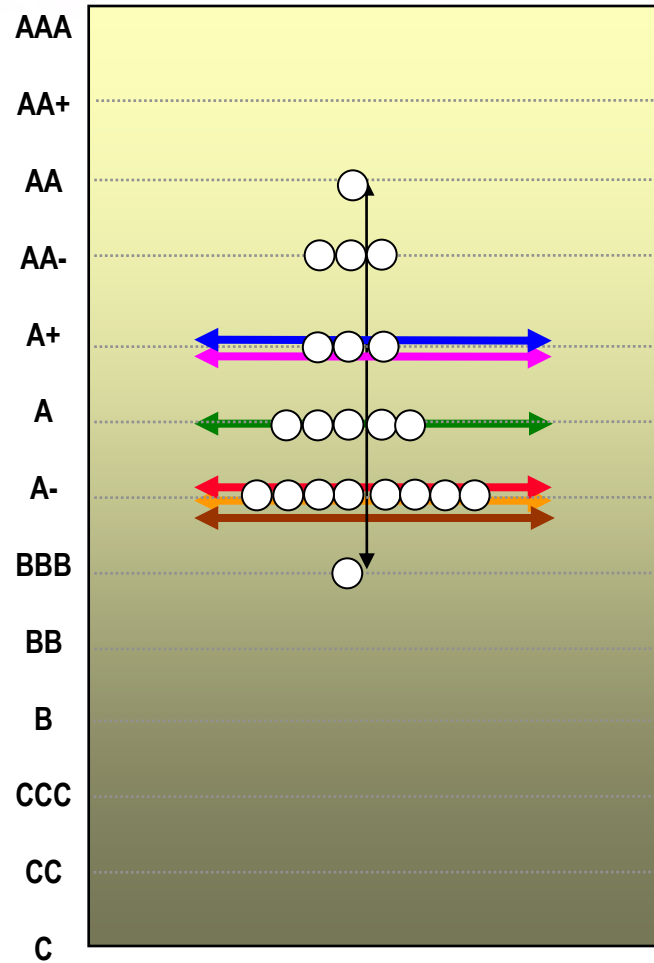


- Asset Commitment Risk - The period of time from when control of securities or cash is given up until receipt of countervalue.
- Liquidity Risk - The risk that insufficient securities and or funds are available to meet commitments; the obligation will be covered some time later.
- Counterparty Risk - The risk that a counterparty (i.e., a participant) will not settle its obligations for full value at any time.
- Asset Servicing Risk - The risk that a participant may incur a loss arising from missed or inaccurate information provided by the depository, or from incorrectly executed instructions, in respect of corporate actions and proxy voting.
- Financial Risk - The ability of the CSD to operate as a financially viable company.
- Operational Risk - The risk that deficiencies in information systems or internal controls, human errors or management failures will result in losses.





Rating



Average Rating - ACSDA
 Average Rating - EU/EEA

Average Rating - Eurasia
 Average Rating - Asia Pacific

Average Rating - Africa
 Average Rating - Middle East

Key Issues

- What is the role of market infrastructure, and CSDs in particular in protecting investors against the next Lehmans or Madoff?
- What lessons have been learnt from the financial crisis?
- If market infrastructure is to take on more responsibility for asset protection, should their business model change?

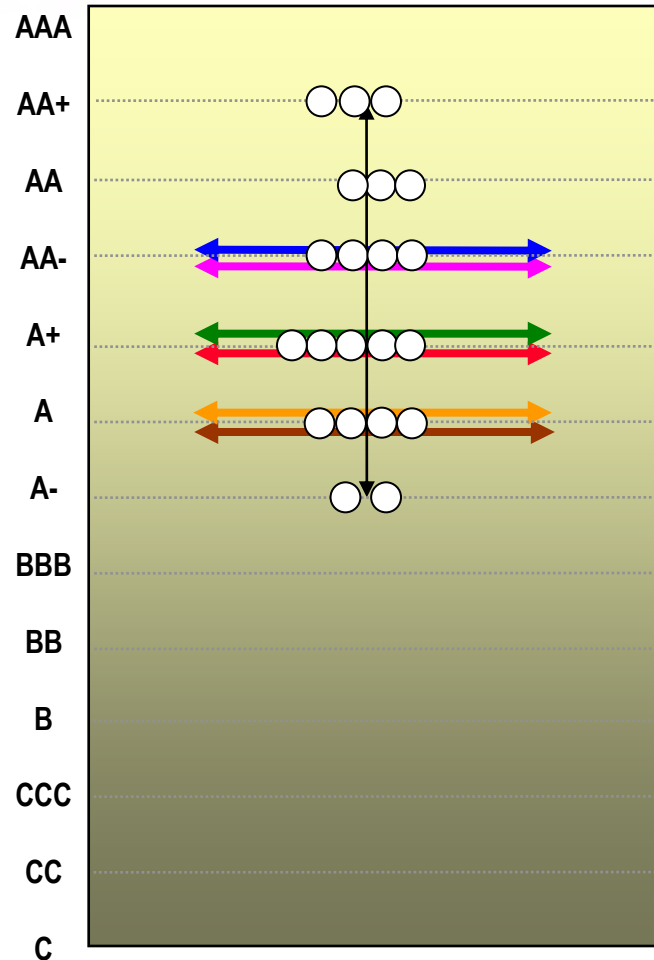
Key Variants: ACSDA vs ROW

- Some ACSDA markets still in the emerging zone and yet to adopt the more recent standards of best market practice.
- However, most CSDs weathered the global financial storm well both from a revenue and risk perspective.





Rating



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Key Issues

- RTGS (normally with optimisation cycles) now common in developed market settlement systems, **but.....**
- Often combined with overnight and or daytime batch routines to maximise liquidity efficiency.
- This flexibility gives participants the choice of optimising liquidity or asset availability.

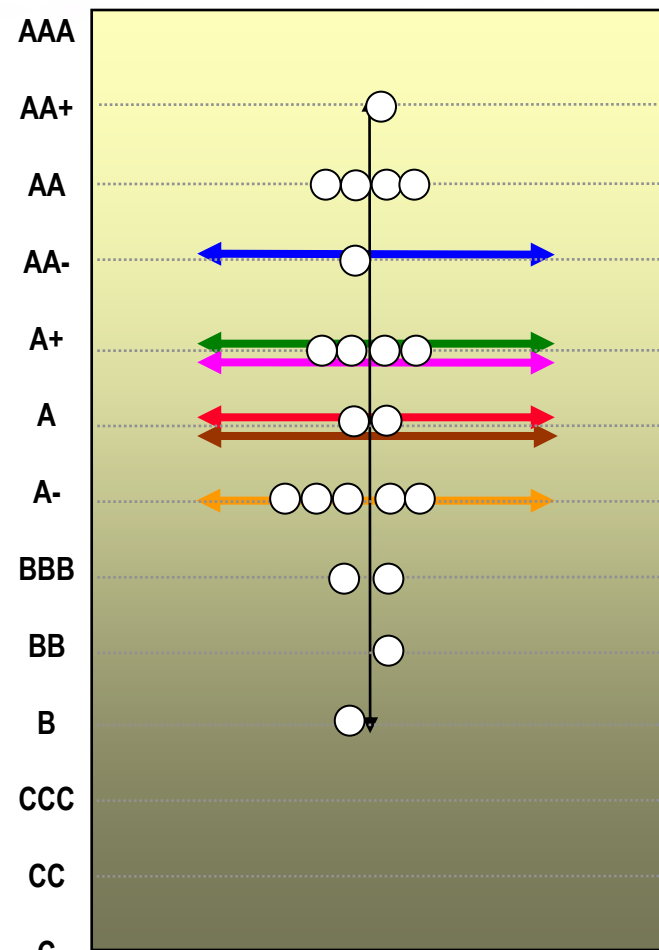
Key Variants: ACSDA vs ROW

- Still a prevalence of batch processing
- Most central banks using RTGS but not linked real time to SSS
- Little blocking or prefunding in contrast to Middle East, Africa and Eurasia





Rating



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Key Issues

- Pressure on liquidity has intensified, and margin and collateral requirements have tightened. How have ACSDA markets responded?
- Widespread bans or restrictions on short selling
- Tightening of credit lead to higher funding costs

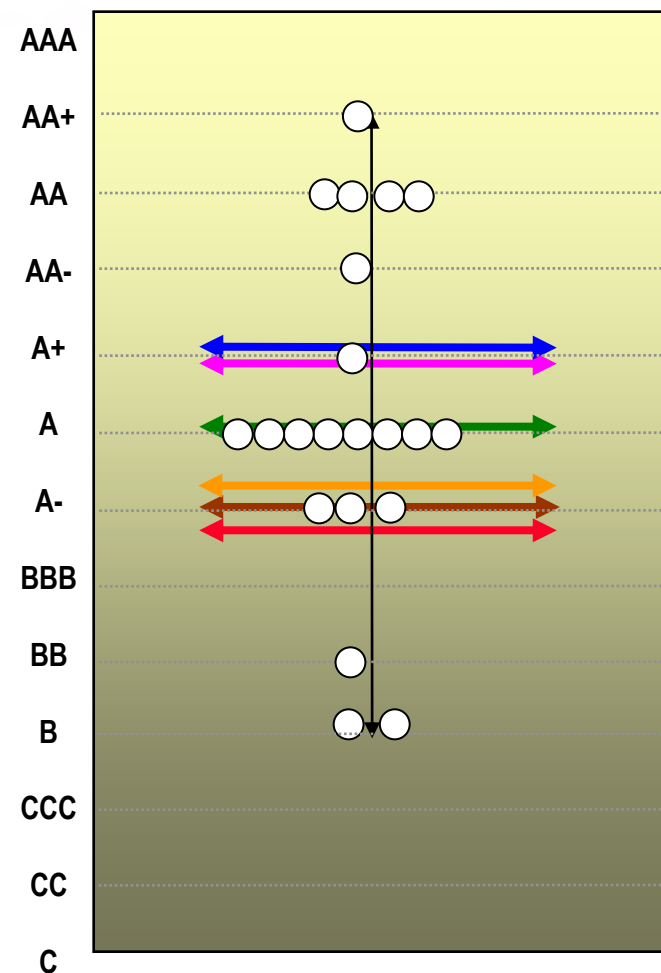
Key Variants: ACSDA vs ROW

- Few ACSDA markets banned short selling (mainly Europe & AP).
- Some ACSDA markets lack developed fails management processes.
- Some ACSDA members lack a critical mass of issued securities under custody leaving much of the market physical.
- Few restrictions on credit facilities for foreign investors and relatively developed interbank lending markets.





Rating



Key Issues

- Counterparty Risk now back on top of the agenda for institutional investors. CCP bandwagon continues rolling.
- How do CSDs that commingle CSD and CCP roles in the same legal entity manage to ringfence the CCP risk?
- How have risk models and participant criteria been adapted since the global financial crisis?

Key Variants: ACSDA vs ROW

- Still a lack of Guarantee Funds and CCPs in the region in contrast to Europe.
- Still a lack of DVP for off-market/ client-side settlement in some ACSDA markets
- Real-time monitoring of participants' exposures (and their collateralisations) is uncommon in ACSDA markets

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 Average Rating - EU/EEA

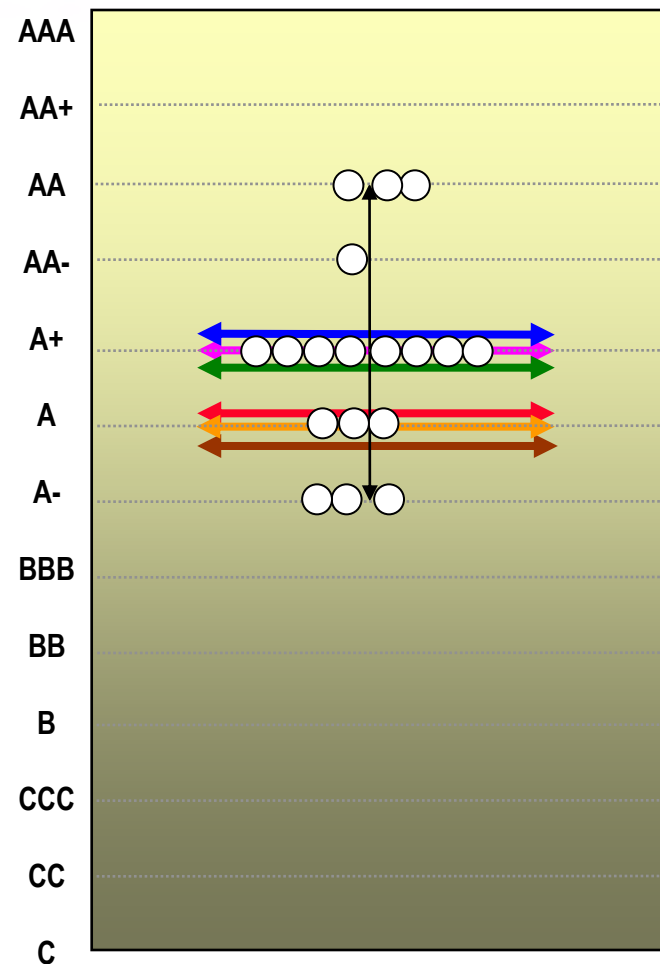
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Rating



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Key Issues

- Expanding business sector for CSDs, gaining ground on custodians
- Does the removal of commercial banking capital from asset servicing disadvantage market participants and investors?
- How have your markets 'de-risked' corporate actions processing?

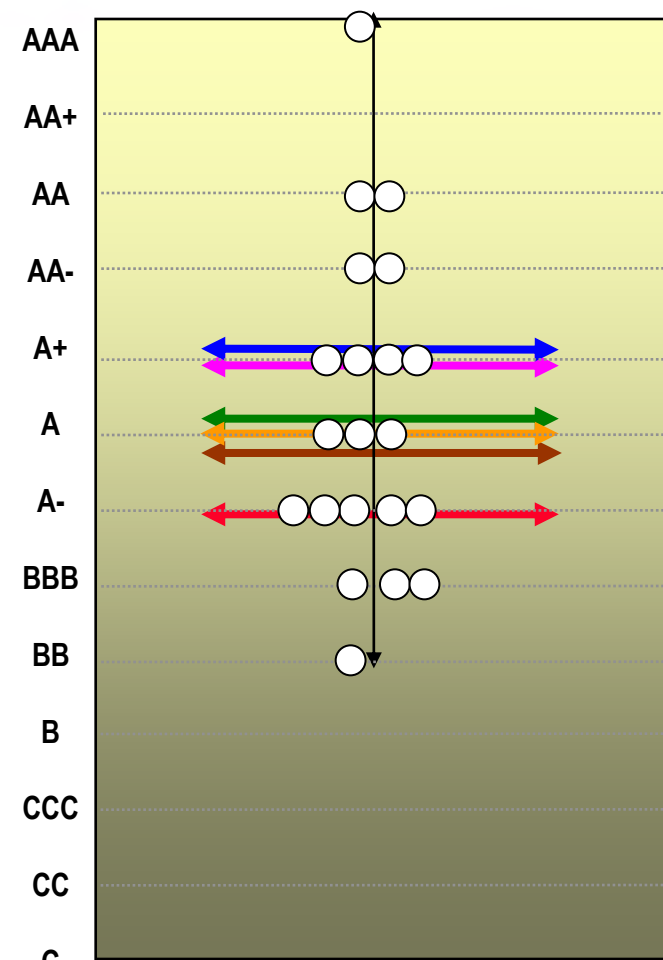
Key Variants: ACSDA vs ROW

- Not all ACSDA members are involved in Asset Servicing to a degree that they are taking on risk exposure
- Where ACSDA members are engaged in Asset Servicing, some have relatively low capital backing this business.
- Few ACSDA members have moved up the value chain enough to threaten to compete with their participants.





Rating



Key Issues

- Adequacy of financial resources a key concern during the recent crisis.
- Many CSDs' profit margins crashed in 2008/9. How have CSDs responded in the short and medium-term?
- How have business models adapted due to the crisis and what lessons have been learned?

Key Variants: ACSDA vs ROW

- Massive diversity in financial resources amongst ACSDA members
- ACSDA members' profit margins not as hard-hit as ECSDA and ACG.
- Still, few ACSDA members have real diversity in revenue streams

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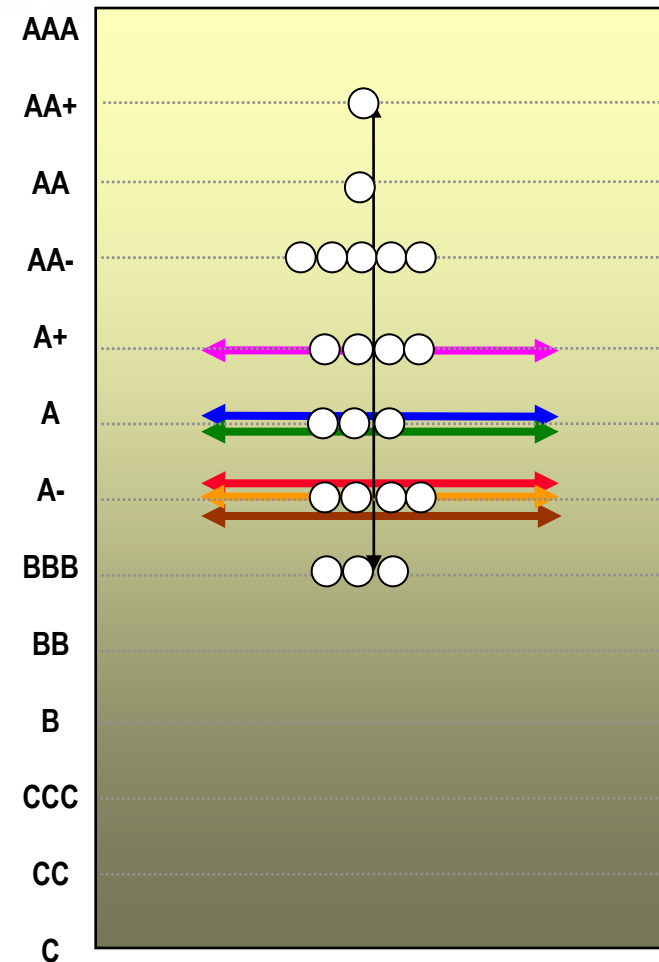
Average Rating - Africa

Average Rating - Middle East
 ○ Still many independent CSDs in the region susceptible to horizontal or vertical consolidation.





Rating



Key Issues

- Adequacy of controls and procedures to maximise asset safety more important than ever.
- Globally, DRP/BCP facilities have been greatly strengthened since 9/11.
- Standardised messaging being more widely adopted by market infrastructure (e.g. SWIFT in Link-Up).

Key Variants: ACSDA vs ROW

- Although ISO certification becoming more prevalent, external operational audits (e.g. SAS70) still rare amongst ACSDA CSDs.
- Relatively low level of 15022 messaging adoption limiting cross-border STP
- DRP/BCP strategies in some markets still need further development.

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