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THE OFFICIAL NEWSLETTER OF THE FIXED INCOME LEADERS SUMMIT 2019

Portfolio trading challenged on best execution

For decades, tourists have flocked to Spain's Costa Brava in anticipation of the three Ss, broadly understood to refer to sun, sea and sangria. At last week's FILS conference, traders flocked to Barcelona to broaden their understanding of how portfolio trading can help them handle another three Ss.

"We're looking to solve for size, speed and sensitivity," said James Deighton, global head of investment grade credit trading at HSBC.

Portfolio trading activity has increased significantly over the past 12-18 months, panellists noted, with most volume seen in investment grade corporate credit, as well as selected other liquid segments of the European and US bond markets.

Lee Sanders, head of execution for global FX and UK & Asia fixed income trading at AXA Investment Managers, said portfolio trading was an important "weapon in the buy-side arsenal", which also gave sell-side firms an opportunity to add value to key relationships, at a time when smaller transactions are increasingly executed electronically on trading platforms.

Sanders said portfolio trades – in which buy-side clients ask banks to execute a basket of 50 or more trades, ▸ 3

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1 ▶ collectively worth upwards of €50 million, for a single aggregated price – could be extremely valuable to buy-side fixed income desks "if we're up against the clock and need instant liquidity". But he later suggested that speed was not necessarily the most significant factor in opting for a portfolio trade, noting the relevance of market direction and information leakage to the decision-making process, and acknowledging the time required to assess risk on a diverse basket.

According to James Chapman, head of credit trading for Europe at RBC Capital, portfolio trading interest from clients covers a "broad church of requests", including rebalancing, tactical adjustments and other forms of risk transfer. In the euro and sterling markets, portfolio trades are typically managed by a single sell-side counterparty, panellists said, with AXA IM's Sanders underlining the importance of discretion on both sides, to enable cost-effective recycling of risk.

But in the larger US dollar market, it is common for buy-side firms to approach three to four banks for prices for portfolio trades. This can be conducted manually, but it is increasingly supported by the major bond trading platforms. According to Iseult Conlin, US credit product manager at Tradeweb, the platform had facilitated portfolio trades in excess of US$1 billion.

"Portfolio trading is still in its infancy in fixed income. As such we're trying to be flexible with the protocol," she said.

Size is not the only reason that the US market is able to support 'in-comp' protocols, said HSBC's Deighton, citing the wider range of hedging options afforded by its deep and sophisticated credit ETF market. "The risk management ecosystem is very different," he observed.

But, at least one delegate wanted to know, can portfolio trades be justified in terms of best execution? Rather than achieving best execution on a line-by-line basis, traders should evaluate portfolio trading in terms of the best outcome overall for the client, said Sanders.

"It may be possible that the bank is unwilling to provide liquidity in a particular bond on an individual basis, but will do so as part of a portfolio trade."

Taking up the risk management theme raised by panellists, a presentation by Brett Olson, head of fixed income for EMEA at iShares, highlighted the growing appeal of bond ETFs to institutional investors. Predicting a doubling in the volume of bond ETFs to US$2 trillion by 2023, Olson cited strategic and tactical asset allocation, and cash and liquidity management, as well as hedging, as factors driving institutional usage. "Asset managers and owners are actively using ETFs in portfolios to make themselves more efficient," he said. ■

QUOTES OF THE CONFERENCE

"The US corporate sector has generated zero earnings growth over the last five years."

Stefan Hofrichter, Allianz Global Investors

"Portfolio trading is still in its infancy in fixed income. As such we're trying to be flexible with the protocol."

Iseult Conlin, Tradeweb

"We have to do a much better job at communicating how we make a positive difference."

Amanda Pullinger, 100 Women in Finance

"Evolution of the primary markets needs to happen."

Mark Bruce, Jump Trading

"Pick the firms that can make the move to electric vehicles."

Mark Wade, Allianz Global Investors

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20
YEARS OF REPO INNOVATION

Warning on credit exposure

There are several cases to argue for reduced credit exposure, noted Stefan Hofrichter, global economist at Allianz Global Investors, speaking on Wednesday at the Fixed Income Leaders' Summit.

While debate over the significance of the yield curve inversion continues, he pointed to another leading monetary indicator, real money growth, and said that this indicator has been coming off sharply over the last three years already while growth rates at a global scale are at levels that in the past have preceded or coincided with a move.

"What I found amazing from the [US] Bureau of Economic Analysis, was that when they significantly revised down the whole economy earnings for the last couple of years, we [found out] that the US corporate sector has generated zero earnings growth over the last five years," he said. "Even though the economy has been growing at rate at or above potential even though we have had significant tax cuts."


Stefan Hofrichter

That is important because in the past negative trends on earnings typically preceded recessions. Margins have come down, which they typically do in the corporate sector well ahead of a hard landing. When see margins are compressed firm reduce spending in reaction to reduced earnings.

Earnings are down because top line growth has been only near 4% while wage growth and labour spend has increased, firms have become highly leveraged.

"The corporate sector is at peak leverage ratios, that to GDP is at the highest level on record and in an environment where economy is coming down and interest cover is deteriorating this is an argument to quite cautious on credit," Hofrichter argued.

He said that in a downturn risk premium starts to steepen, which means the industry will expect not only credit risk to be repriced but also the yield curve to steepen again going forward. ■

Could 'Fortnite' guide market evolution

Online game 'Fortnite', Netflix and Spotify will drive technological advances in e-trading, Steve Toland, founder of TransFICC, told delegates at the Fixed Income Leaders Summit this week.

Toland said the tech used by the gaming and online video and music streaming industries was relevant to the development of e-trading systems for fixed income traders.

"Fortnite has different players competing against each other in real time all over the world. If one player is milliseconds behind another, they will be at a competitive disadvantage which is not unlike traders competing for the same prices on central markets," Toland said.

The 2019 Global Internet Phenomena report published by Sandvine, found Netflix accounted for 12.6% of total downstream volume of traffic across the entire internet and has a presence in 190 countries servicing 155 million customers. Toland argued that fixed income traders needed access to the same level of service afforded to the biggest streaming services if they are to compete on the global digital stage.

"How did Netflix get to 190 countries? It uses Amazon Web Services which is cloud computing technology. This gives them the ability to send information in real time to the cloud as demand comes in, which is how Fortnite was able to grow from zero to 10 million users in one month."

Toland said e-trading would need to emulate the gaming and streaming companies in employing small, co-located teams of developers who were expected to regularly release new technology.

"Co-located engineers working closely together to develop proprietary systems is the most effective way to work," Toland said.

Finally, Toland said traders should ask how developers are organised; what open source technology is used; what is the plan to migrate to the cloud; is an automated testing approach in place; how often the developers release to production and whether regulatory issues were considered during the build. ■

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Fear that 'diversity washing' could limit progress

Mark Wade, head of credit research at Allianz Global Investors, has accused the financial services industry of 'diversity washing', during a debate about inclusivity held at the Leaders in Fixed Income Summit this week.

During an All Star Panel which aimed to 'tackle the diversity issue head on', Wade said financial services companies were not doing enough to change the make-up of their senior management teams.

"There is a lot of talk in our industry about green washing when it comes to environmental social and governance investing, but you could say there is some diversity washing too. There is a lot of rhetoric about how nice it is when a woman is appointed [in a senior role] but that means we are still looking at the gender and not the person," he said.

Wade added that asset managers had not done enough to change company cultures meaning women in junior roles often found it hard to relate to counterparts who had reached the top.

"I have spent part of my time talking to women in different regions and roles, and there was often no degree of relatability between them and those women who were winning the top jobs. They didn't feel that there was enough change in the culture."

He added: "If I asked whether they felt their probability of reaching

Amanda Pullinger

[senior management] had improved over the five years, they said at best it was marginal but more probably it was flat."

Wade said that the challenging economic environment had led many asset managers were reducing their head count, meaning the only way to ensure to improve diversity was to 'have fewer people of a certain type' on the payroll.

However, Wade argued that it was difficult for asset managers to justify changes to their senior teams.

"[Asset managers] need is to overhaul the way we operate on day to day basis and reshape some of the long-standing legacy structures. Yet, If I talk to a client the first question I am asked is 'has there been any turnover in staff?' Clients want people to work at the same desk for 70 years with no change. There are some structural weaknesses in our business that are preventing change," Wade said.

Fellow panellist Amanda Pullinger, CEO of 100 Women in Finance, warned that unless asset management businesses started to make significant efforts to be more inclusive, they risked losing out to their tech competitors in the battle for talent.

"[Asset managers] are perceived by the next generation – male or female – as an industry that is self-serving; making rich people richer. We are fighting the technology industry for this talent and we have to do a much better job at communicating how we make a positive difference to the lives of ordinary people," Pullinger said.

Pullinger said 100 Women in Finance was launching an initiative called maths for girls that would see female portfolio managers go into schools to promote the industry.

However, Wade questioned whether the focus should be so heavily weighted to maths, arguing that asset managers needed to encourage people from different backgrounds with a range of skillsets.

"I really don't need my A-level or degree in maths," Wade said. "If you are in research it helps to be able to do sums in your head, but marketing, sales and compliance roles don't need maths. We need to broaden [diversity strategies] out to think about the skillsets required to help the business outperform." ■

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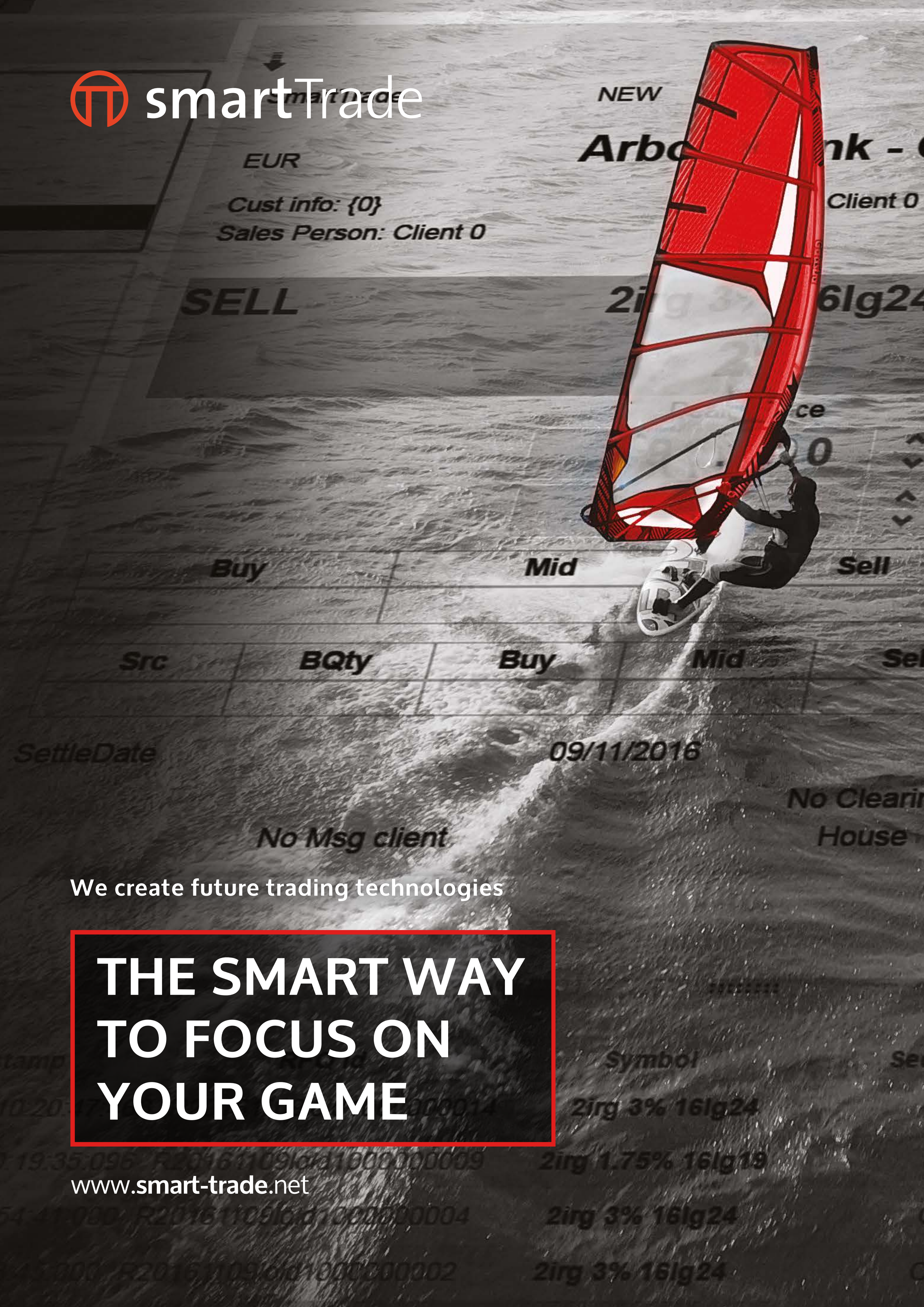
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CIOs assess stormy markets ahead

Managers can expect an even worse start to 2020 than they endured in 2019, unless credit markets see an adjustment, according to Chris Iggo, chief investment officer at AXA Investment Managers.

Iggo, who was participating in the CIO keynote interview on the second day of the Fixed Income Leaders Summit in Barcelona, warned of challenging months ahead.

He said: "Unless credit weakens in the next few months then we will be starting 2020 with lower yields than we started with in 2019. That means total return expectations will also be lower than they were last year."

Iggo said AXA IM would continue with its strategy of diversification in fixed income, with a preference for high yield credit and emerging market debt.


Chris Iggo

He added: "[This year] we were lucky enough to get the call right on rates and being long duration has been good for us. It pays to be long duration when markets are going through volatile times and that will remain core going forward."

Fellow CIO, Rick Lacaille of State Street Global Advisors, agreed with the need for diversification in the coming months as the industry moves into 2020. He also advised investors to look out for 'blind spots' in the fixed income markets.

Lacaille said, "Investors need to be diversified but should keep an eye on the radar screen for opportunities that pop up because of investor disagreement. Investors need to be selective and look for where there is a potential blind spot such as in emerging market debt, where dollar-based investors shy away from the risks of foreign currency exposure."

He added that the challenges associated with the ongoing Brexit negotiations, meant investors needed to ensure they had necessary liquidity.

"The question is whether you will get through this [period of instability] as an investor or will you be derailed? During such conditions, liquidity is important in fixed income portfolios," he said. ■

9Fin takes the win in Dragon's Den

Financial technology (fintech) firm 9Fin won the 'Dragon's Den' event at FILS 2019, beating tough competition from Auquan and Scorable.

Following a series of pitches for each idea, the judges grilled Steven Hunter, co-founder and CEO at 9fin, Oliver Kroll, chief product officer at Scorable and Chandini Jain, CEO at Auquan about how their products work and what they solve.

9Fin uses machine learning to gather and consume, then organise and understand financial data in the fixed income markets. Pulling it into one place effectively makes it easier to search, filter and analyse. This is both an efficiency play through time saving, but also allows professionals to potentially spot big market events before they happen. The firms claims to have predicted more than 20 price sensitive market events this year to date.

Scorable also uses artificial intelligence (AI) but to analyse credit risk in bonds based on multiple data sources such as financial news, market prices and credit ratings, with are then set against their influence on a company's financial position. This is also aimed at predictive support for investors.

Kroll said the firm had an 80% true positive score rate on predicting downgrades – and non-downgrades – over a 12 month time horizon.

Auquan uses a collective of data


Julia Streets & Steven Hunter

scientists to crowdsource trading strategies; by allowing portfolio managers to put problems out to a group of data scientists, the latter get payment and recognition for their achievements and the former get solutions to investment problems. ■

Electronic liquidity providers push for reform

The buy side relationship with alternative liquidity providers was strained five years ago after the high-frequency traders and their reputations – and business models – were implicated in structural bias in Michael Lewis's 2014 best-seller 'Flash Boys'.

This not-so-new generation of market disruptors has long been rehabilitated in the equities markets, with buy-side traders gradually becoming more savvy and sophisticated in how they source liquidity. In the fixed income world too, electronic liquidity providers are now seen as valuable and viable counterparties reflected by two presentations on Wednesday morning.

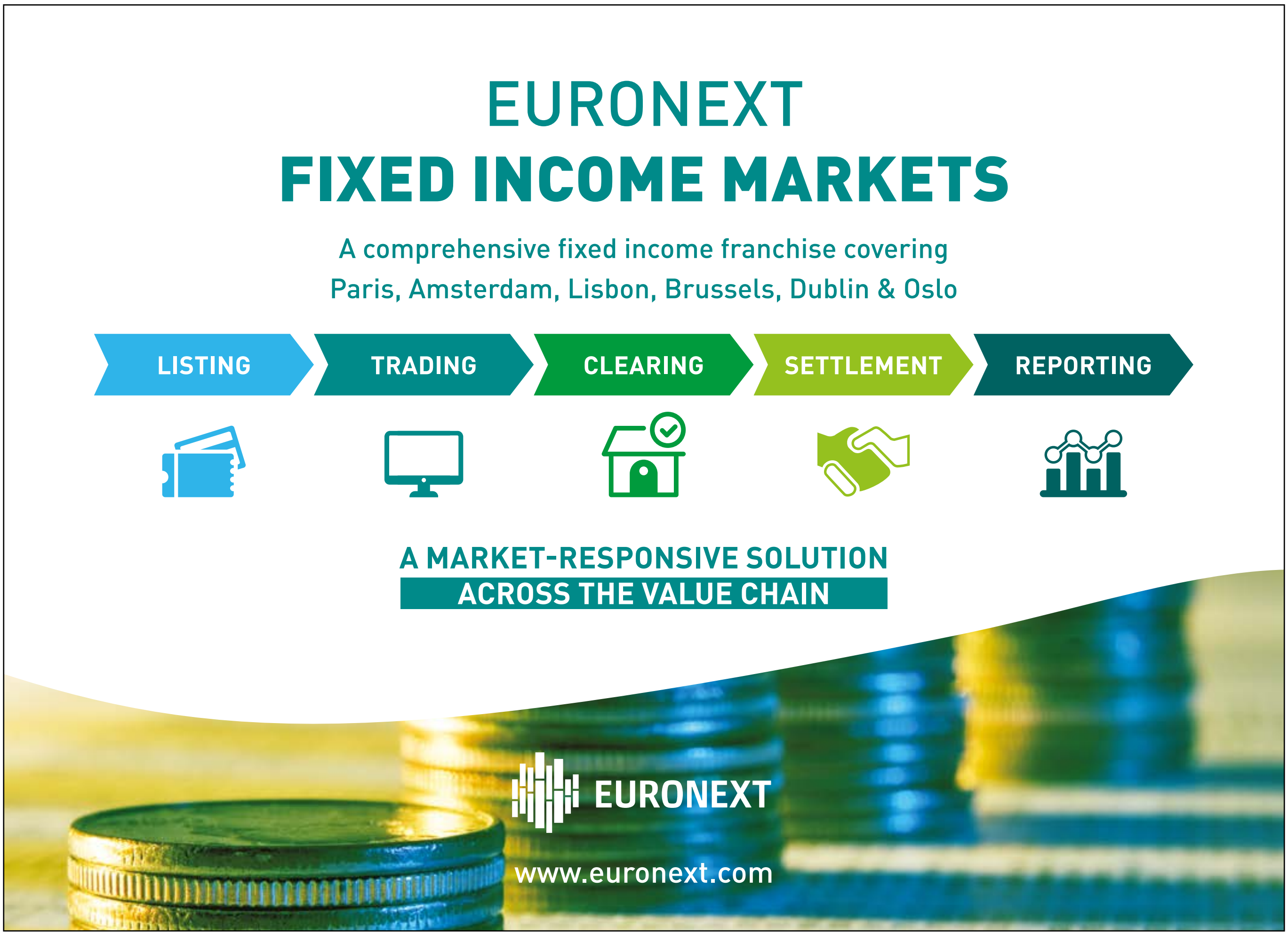
First, Mark Bruce, head of FICC at Jump Trading, explained how his firm and others are increasingly supplying bespoke and bilateral liquidity to large buy-side players in the US Treasuries market, via the direct streaming services of electronic trading platforms.

Now that asset managers are sourcing substantial and consistent levels of liquidity from Jump Trading, the firm is looking to expand its offering, by streaming blocks and making markets in European government bonds. Bruce said the firm hope to overcome existing access limitations.

"Evolution of the primary markets needs to happen," he said, to enable direct streaming in Europe.

As outlined by global head of fixed income trading Matt Berger, Jane Street's increasing levels of interaction with the buy-side are being driven largely through the exponential growth of portfolio trading. According to Berger, the firm facilitated US$22 billion in portfolio trades in Q3 2019, a more than fivefold increase over Q3 2018.

The firm's ability to offer tight spreads on portfolio trades stems partly from the overlap with its ETF business, but Berger said continuous innovation was necessary to meet evolving demand, from both passive and active managers. "Increasingly, there are portfolio trading solutions for a broad number of buy-side firms. We're working with clients to make the process smoother and more efficient," he said. ■



Funding the green transition

How on God's green earth are fixed-income portfolio managers supposed to negotiate the minefield of sustainable investing, given the myriad pitfalls and bear traps that can frustrate the most ethical of intentions?

This was the central issue tackled on Wednesday afternoon's portfolio management session, 'ESG and Impact investing'.

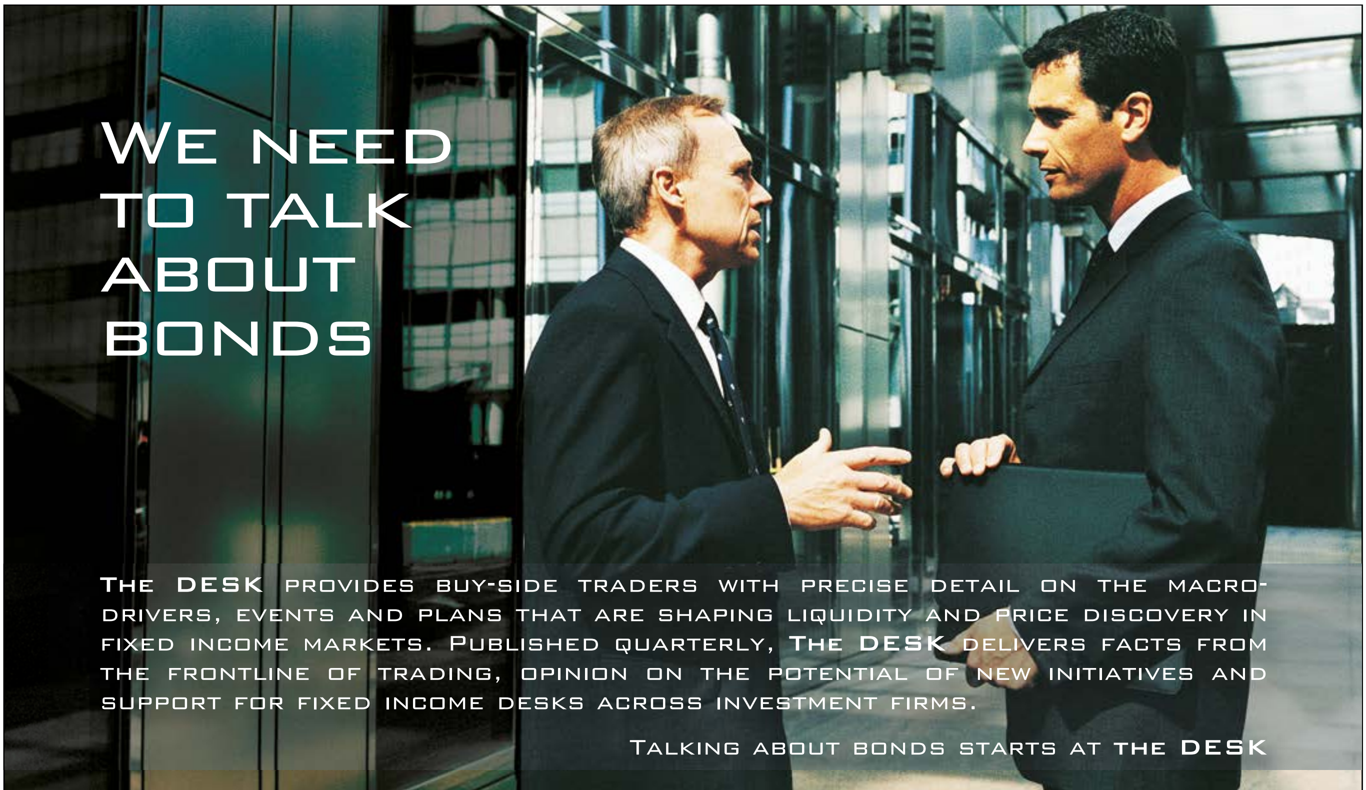
Bryn Jones, head of fixed income, Rathbones Investment Management, admitted that topics such as investment in nuclear energy could lead to "difficult conversations" with investors. Nuclear power does not contribute to global warming and does not produce carbon emissions, but "when it goes wrong, it goes very wrong", observed Jones, who manages the Rathbone Ethical Bond Fund.

In this complex and fast-evolving environment, Jones advocated active engagement by investors with issuers, providing feedback on their strategies and explaining the kinds of disclosure they seek.

Mark Wade, head of credit research at Allianz Global Investors, said that one area often overlooked by those wishing to prioritise green investments is the need to support firms transitioning from traditional to sustainable business models. Noting that some investors are pivoting away from the automotive sector, due to the associated consumption of fossil fuels, Wade called for funding support for those traditional manufacturers most able to execute on change. "Pick the firms that can make the move to electric vehicles," he said.

Even investing in electric vehicle production is fraught with tensions, admitted panellists, pointing out the challenges of sourcing 'rare earth' minerals used in the production of storage batteries.

Responding to an audience question on how the sell side can support sustainable investment, Wade encouraged banks to help corporate clients in "fronting up" on matters of sustainability, for example providing detailed documentation around issuance. Clients would be rewarded with a falling cost of capital, claimed Wade, whose point was supported by Jones, with reference to diverging funding costs in the energy sector. ■



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Fixed income trading

A look at current market challenges and the leading-edge tools that can mean the difference between success and failure.

Trusted data is the lifeblood of the fixed income trading desk, but as Refinitiv's Alexandre Hardouin explains, data alone is not enough – traders also need the right tools to make sense of vast quantities of incoming information if they are to make sound decisions with accuracy, speed and precision.

The fixed income data explosion: opportunities and challenges

The fixed income arena in recent years has been characterised by a literal explosion in the availability of market data. Whilst more data offers fixed income traders unrivalled opportunities to better their strategies and performance, vast quantities of incoming data also create new challenges.

Driven by new technology and the rise of electronic trading, the swelling tide of available information and the move towards live prices replacing indicative bids have resulted in greater price transparency, but on the flip side, traders cannot afford to miss any important nugget of information.

They are therefore tasked with constantly revising their overall view of available opportunities, often at speed. It is here that too much information can become a double-edged sword, because pinpointing and accessing the most relevant data sets can quickly become complex and time-consuming.

A new Refinitiv whitepaper, *Defining Fixed Income Data – The Value of Centralizing and Normalizing*, available at **refinitiv.com/defining-fi-data**, takes a deep dive into this burgeoning availability of fixed income data and offers critical insights into the attendant challenges and opportunities.

The paper specifically highlights the challenge of numerous data types, but more than this, the fact that data sources are often fragmented, meaning that market participants may need to engage several data providers, multiple trading platforms, and different regulatory bodies in order to form a complete market view.

Another core challenge centres on data quality. It goes without saying that traders should trust the data on which they base their most crucial decisions, but not all datasets are equally reliable.

Moreover, in the interests of boosting speed and efficiency, fixed income players need to find cost-effective ways to automate the flow of information.

Comprehensive solutions: a one stop shop

Given this set of on-the-ground challenges, Refinitiv has developed and refined a set of tools and solutions that can offer significant help to traders as they strive to access quality data, make sense of this data, improve their efficiency and ultimately make better decisions.

We offer a comprehensive range of fixed income data, and through our various partnerships with other fixed income players, we have expanded the scope of our offering beyond our own content and data to include some of the best-in-class solutions available on the market.

A snapshot of our solution universe follows:

- Eikon, built on open platform technology, delivers trusted news, data and analytics, filtered to the end-user's exact requirements. The platform connects users to markets and professional networks and offers traders the ability to view prices from different multilateral trading facilities (MTFs), including Tradeweb and MarketAxess, as well as MiFID II reported data. This exclusive data set is unique in the fixed income market. Eikon can be accessed via desktop, over the web, or on mobile devices.
- Our Elektron Data Platform is an integrated content and capabilities solution that enables users to access data and analytics and integrate their own data – all on a single platform. Elektron delivers real-time, reference, end-of-day, time series, and alternative data, along with powerful analytics solutions. Data is cleaned, tagged, and standardised to enable end-users to spot the linkages, relationships, and connections that enable a holistic view of available opportunities. Data is distributed via feeds, direct to your desktop or applications from the cloud,

or via hosted or managed data management services.

- IFR Markets delivers across-the-board fixed income, global credit markets and currencies coverage, including major government bond markets, investment-grade credit, high-yield, emerging markets, mortgage and asset-backed securities, interest-rate swaps and major FX pairs. IFR Markets content is available on Eikon and features integrated news flow and our New Issues Monitor, which delivers new issue information from pre-marketing to price guidance to final pricing and commentary.
- In addition, our 2018 partnership with valantic saw a new strategic combination of Eikon and valantic's iQbonds, which delivers market making and pricing capabilities for fixed-income products with connections to electronic markets, exchanges, and information platforms. This new integrated solution enables full coverage of the fixed income sell-side trader workflow to boost efficiency. Fixed income traders can now answer incoming RFQs at speed and simultaneously ensure that bank and market prices align.

Support for fixed income traders

Refinitiv conducts regular research into the trends and challenges inherent within the fixed income market and we tailor-make our solutions to address these challenges.

We have the breadth and depth of fixed income content and data necessary to offer real and tangible support to fixed income traders and consistently deliver accurate, trusted data. As the exclusive vendors of many of our best-in-class partner fixed income data sets, we are able to meet the full range of fixed income data and pricing needs.


Alexandre Hardouin

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- Interdealer broker rates and money market data such as IRS (including 19901 ICAP swap data), currency basis swaps, OIS, FRA, and single currency basis swaps;
- Exclusive loan data from *Loan Pricing Corporation;*
- Exclusive bond holding data from *eMaxx;*
- Access to CDS instruments through *Markit* and Refinitiv for single names, indices and sectors;
- Powerful real time analytics such as zero curves, swaption skews, OIS curves, credit curves, issuers curves, and RPS bond data;
- Access to *Starmine* credit risk model;
- Easy to use Eikon pre- and post-trade apps help you leverage market insights – apps include *All Quotes, Rates Views, New Issue Monitor, Bond Calculator, Swap Pricer*, and *Multi-Asset Risk & Valuation.*

This vast array of data can also be fed into your own third-party desktop applications to streamline the flow of data through your workflow, allowing you to power all your third-party desktop apps with Refinitiv data, and ensuring the same data is captured across all your applications.

A final word

As the availability of data in the fixed income space continues to grow, market players should continually evaluate the universe of new tools and solutions that are available to support and simplify decision-making.

More information can deliver many benefits, including enhanced transparency, but not without attendant challenges. Innovative thinking and new solutions, however, can cut through complexity. To this end, Refinitiv remains committed to the open sharing of quality data and to supporting the ongoing transformation of the fixed income market to the benefit of all stakeholders. ■

About the author

Alexandre Hardouin manages the Refinitiv product proposition for fixed income markets globally, driving the strategy to serve both sell-side and buy-side market participants. Alexandre worked as a Sales Trader and in a financial software start-up prior to joining Refinitiv (then Thomson Reuters). He then pursued a 15-year career in client facing and product management roles with specific expertise in fixed income markets.

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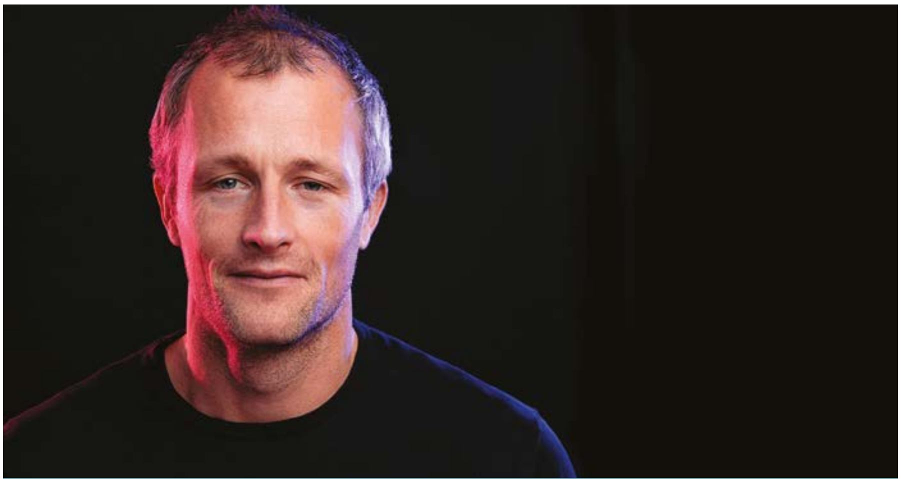
How to overcome the hidden challenges of new derivatives regulation

By Peter Rippon, CEO, OpenGamma

New regulation introduced to mitigate the systemic risk associated with both cleared and uncleared OTC derivatives has also brought about additional costs and challenges for firms trading these products. The preparatory difficulties are clear: lengthy negotiation of legal documentation, custodian selection, margin calculation models and collateral mobilisation. However, there are much bigger challenges that will present themselves further down the line once these rules kick in. Firms do have an opportunity to adapt to the longer term impact of new regulation, and those that do will to achieve competitive advantage.



"Through replicating the complex margining models that regulatory risk-based margining models now demand, firms are able to validate margin calls and mitigate operational risk created under the new rules."

Dramatically lower portfolio liquidity

More liquid assets are now required to be posted as collateral for derivatives positions under new regulation, sucking liquidity out of firms. This results in more assets having to be held in lower yielding securities and low yielding cash. As a result, this has magnified the importance of actively managing portfolio liquidity, especially so in periods of higher market volatility.

Visibility into the impact of new rules on portfolio liquidity is now available through advanced analytics which can forecast the future margin requirements. Big-data paired with smart analytics can support the tricky new balancing act involved in maintaining liquidity while minimising the drag on returns.

Significantly more operational exposure

With the increase in the number of margin calls – and subsequent increase in complexity surrounding them – the probability of incorrect calls has increased dramatically. Posting excess margin is, firstly, highly inefficient from a cost perspective. Plus, there is an inflated operational risk from failing to ensure that the right amount of investor assets are being posted as margin.

However, technology is available to minimise the new risks inherent in this process. Through replicating the complex margining models, firms are able to validate margin calls and mitigate operational risk created under the new rules.

To sum up

With Phase V of UMR being moved back from September 2020 to September 2021, firms really should be using this time as an opportunity to look beyond only the 'must have' operational requirements to the longer term impact that these rules will have on both return and liquidity.

The reason the delay was agreed upon was due to the struggle firms were finding in meeting the original deadline, so it is imperative that – rather than resting easy – firms use the extension to prepare themselves for the less obvious longer term impacts of these regulations. ■

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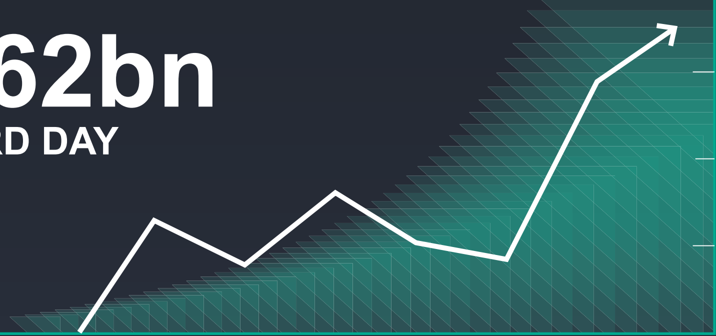

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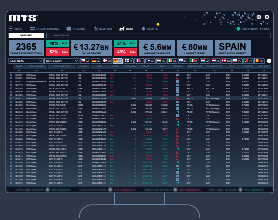

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