



THOMAS MURRAY

Fails Management Models

AMEDA 16<sup>th</sup> Meeting

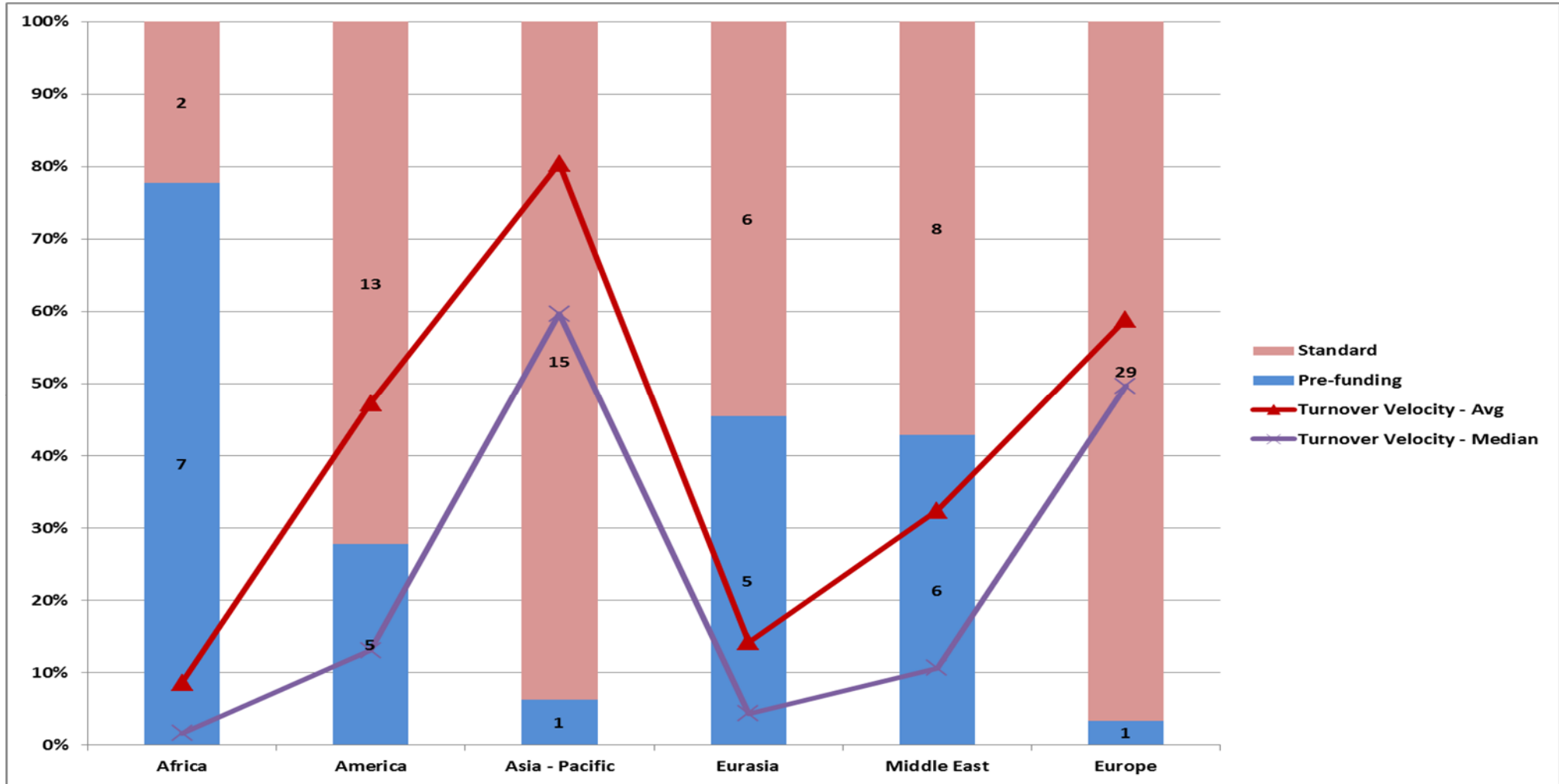
Kuwait, 26-29 November 2012

## Agenda

- Pre-Funding Model
  - Trends
  - Pro's & Con's
  
- Fails Management Mechanisms
  - Fails: reasons and mitigation tools
  - Buy-in Practices
  - Penalty Schemes
  - Securities Lending Practices

# Pre-Funding Model

## Trends Across Regions



Pro's	Con's
<ul style="list-style-type: none"><li data-bbox="256 486 899 586">• No Fails from lack of securities or cash</li><li data-bbox="256 654 754 704">• No Short Selling possible</li></ul>	<ul style="list-style-type: none"><li data-bbox="1023 486 1707 586">• High settlement liquidity demand for participants</li><li data-bbox="1023 654 1742 753">• Securities blocked from TD to SD and not available for re-use</li><li data-bbox="1023 821 1715 921">• Not convenient for Foreign Investors from different time zones.</li><li data-bbox="1023 988 1694 1088">• Ensure link with Stock Exchange is solid</li><li data-bbox="1023 1155 1686 1255">• Dependent on the Exchange being open</li></ul>

# Fails Management Mechanisms

## Fails: Reasons

### 1. Lack of Securities

- No timely delivery of securities
- No sufficient securities available at the cut-off time

### 2. Lack of Cash

- No timely delivery of funds
- No sufficient funds available at the cut-off time

### 3. Matching Issue

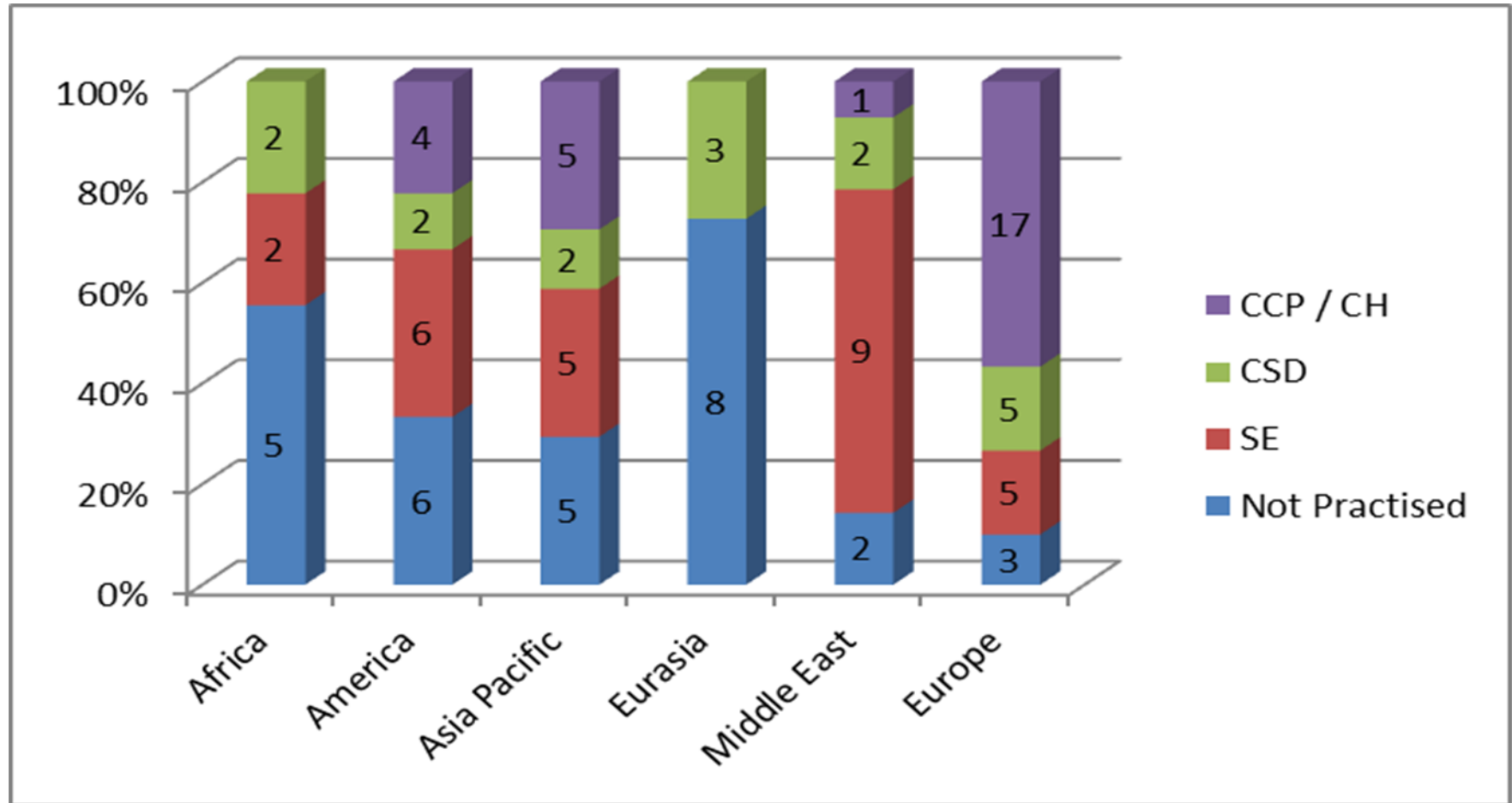
- Incomplete / inaccurate instructions
- Missed deadlines

## Fails: Ways to Reduce / Mitigation Tools

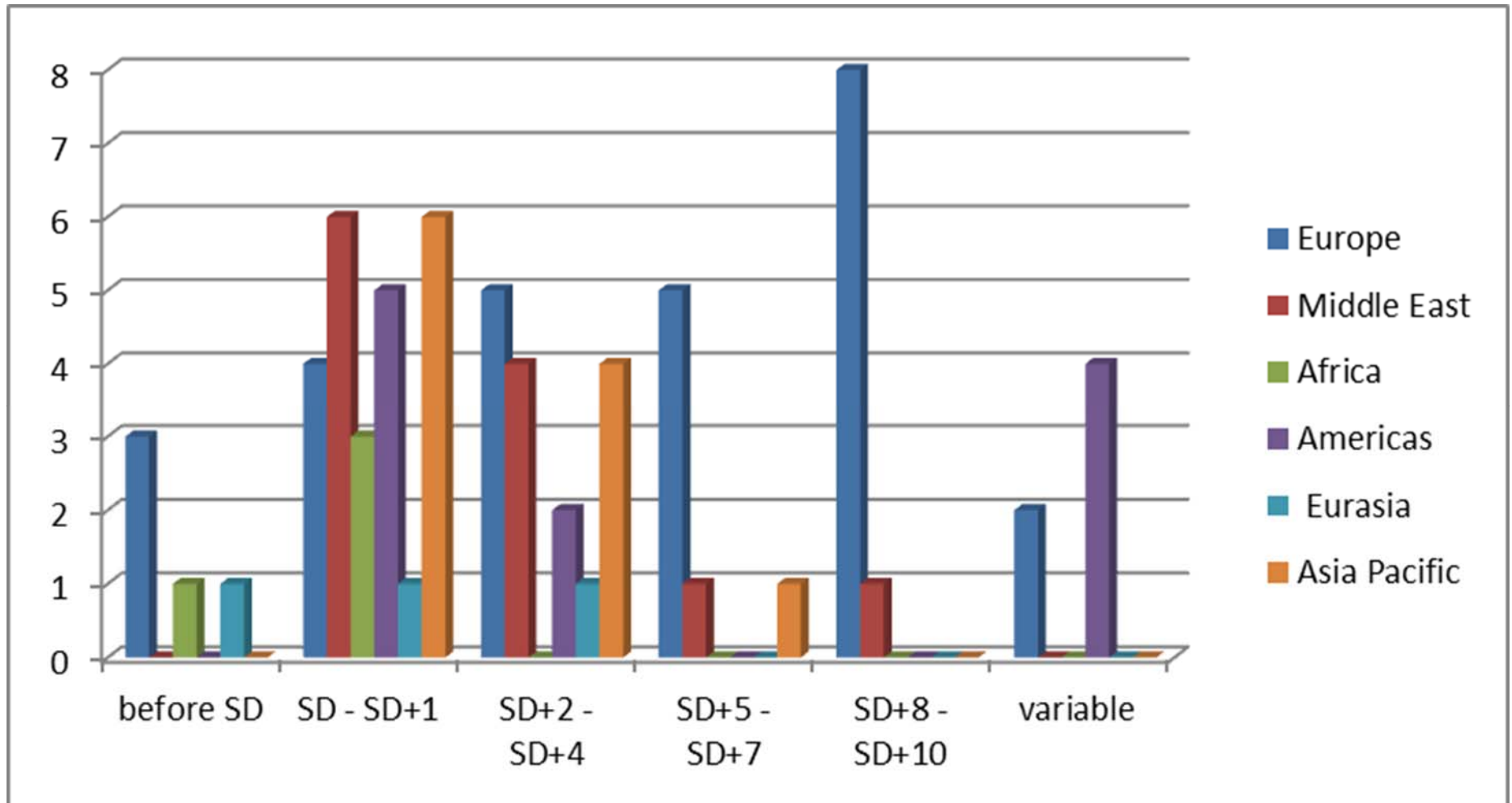
	Lack of Securities	Lack of Cash	Matching Issue
TD           SD   ▼ SD+n	<ul style="list-style-type: none"> <li>• Securities Lending</li> <li>• Reverse Repo market</li> <li>• Efficient Netting (CCP)</li> </ul>	<ul style="list-style-type: none"> <li>• Credit facilities from Banks</li> <li>• Automated facility with Central bank</li> <li>• Repo market</li> <li>• Efficient Netting (CCP)</li> </ul>	<ul style="list-style-type: none"> <li>• Longer settlement cycle</li> <li>• Pre-match instructions</li> <li>• Tolerance Limits</li> <li>• Bilateral Cancellations</li> <li>• Hold and Release Mechanism</li> </ul>
	<ul style="list-style-type: none"> <li>• Buy-ins</li> <li>• Penalties</li> </ul>	<ul style="list-style-type: none"> <li>• Sell-outs</li> <li>• Penalties</li> </ul>	<ul style="list-style-type: none"> <li>• Automatic recycling of instructions</li> </ul>



### Buy-in Practices



### Buy-in Timings



## Penalty Schemes

### Mandatory – Daily

- Fixed fee
- % of transaction
- Fixed fee + % of transaction

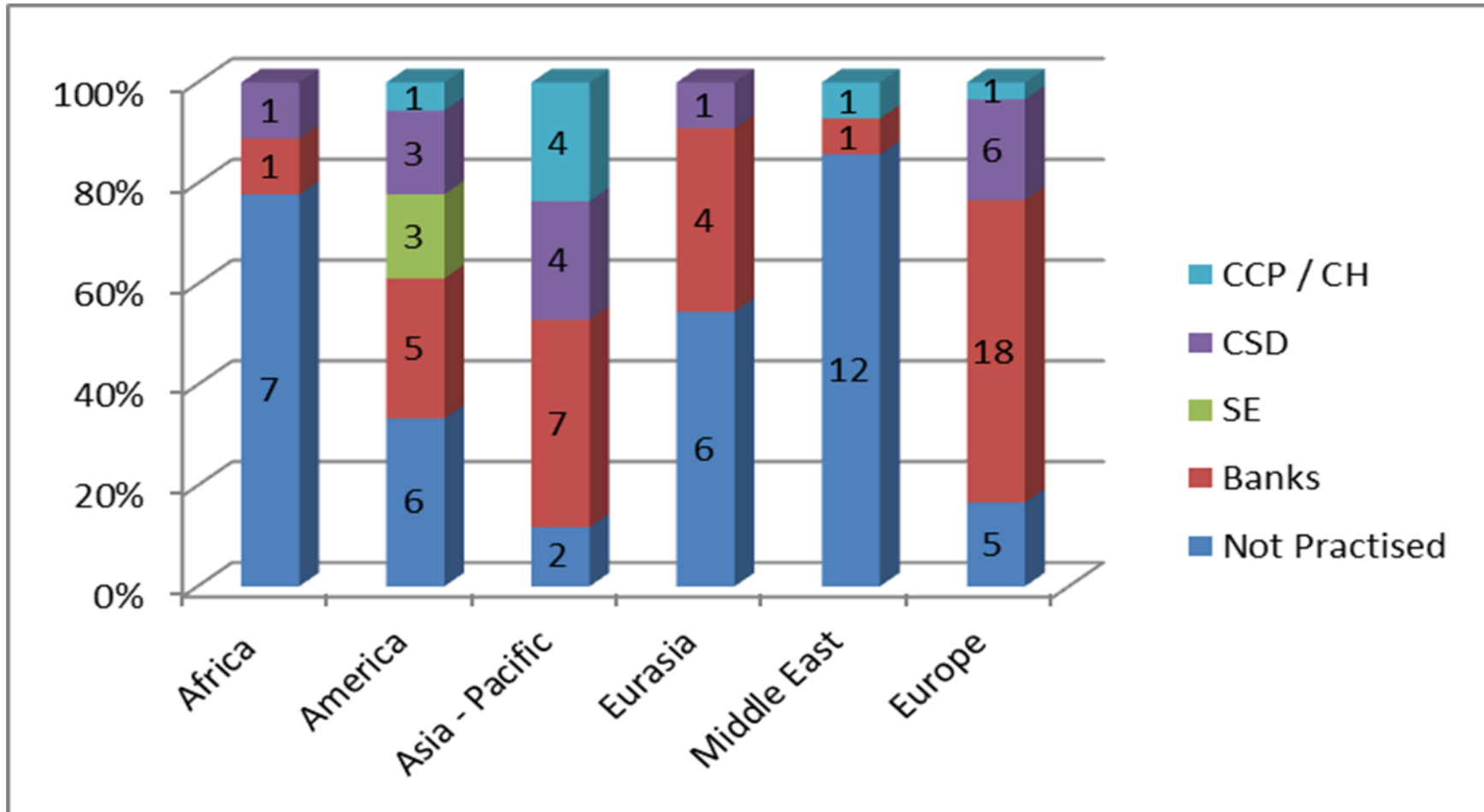
### Subject to DPs Behaviour

- Charged (e.g. monthly) on participants with low settlement rate

### Subject to Market Behaviour

- Charged only if the overall rate reaches a certain threshold.

## Securities Lending Practices



## Conclusion

- Pre-funding models are used mainly in emerging markets to control counterparty risk.
- High trading liquidity does not seem compatible with pre-funding models.
- Adequate fails management mechanisms and regulations in developed markets show that fails can be monitored and dealt with.

# Thank You