

CASLA Conference 2013

Fixed Income Panel Discussion

May 8, 2013



CASLA 2013: FIXED INCOME PANEL DISCUSSION

Panelists

Chris Tigert

- Director, Fixed Income Securities Lending, CIBC Mellon

CIBC MELLON

Oscar Huettner

- Director, Global Product Manager, BondLend



Bob Nobrega

- Portfolio Manager, Ontario Teachers' Pension Plan



Gord Pearce

- Managing Director, Securities Finance, RBC Capital Markets
- CASLA Director



RBC Capital Markets

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Topics for Discussion

Collateral

- Securities Lending Programs
- The Evolution of the Repo Market in Canada
- Increased Foreign Sector Participation in Canada
- The Shrinking Pool of “AAA” rated assets
- The Growing Demand for High Quality Collateral in the Marketplace

Repo Strategies in a Fixed Income Portfolio

- Generating Returns in a Period of Low Interest Rates and Low Volatility
- Repo is becoming an increasingly important instrument for Canadian Pension Plans
- What is the Impact on the Repo Market?

CDCC Fixed Income CCP

- A Brief History
- Where We Are Today
- Next Steps

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“The securities-lending market facilitates an increase in overall market liquidity and in the flexibility of financing. It promotes market efficiency by enhancing the price-discovery mechanism in cash securities markets. For these reasons, and because of its role in supporting market-making activities, the securities-lending market has been identified by the Bank of Canada as one of the five core funding markets.”¹

*“The Role of Securities Lending in Market Liquidity”, Nadja Dreff
The Bank of Canada Financial System Review, June 2010*

¹ The other core funding markets are: (i) the market for Government of Canada treasury bills and bonds; (ii) the repo market; (iii) the market for bankers' acceptances; and (iv) spot and swap foreign exchange markets.

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The Workstream has identified the following five key drivers of the securities lending and repo markets:

- 1. Demand for Repo as a Near-Substitute for Central Bank and Insured Bank Deposit Money*
- 2. Securities-based Financing Needs*
- 3. Leveraged Investment Fund Financing and Short-Covering Needs*
- 4. Demand for Associated ‘Collateral Mining’ From Banks and Broker-Dealers*
- 5. Demand for Return Enhancement by Securities Lenders and Agent Lenders*

*“Securities Lending and Repos: Market Overview and Financial Stability Issues”
Interim Report of the FSB Workstream on Securities Lending and Repos*

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As it stands globally, since the time the Great Recession took hold in 2008, we have seen the total value of government debt backed with AAA-ratings decline from over a 50% share of total outstanding sovereign credit to less than 10%. Quality is scarce, and as such should be owned.

David Rosenberg, Chief Economist & Strategist
Gluskin Sheff + Associates, May 2012

Canada is but one of 11 sovereign credits with a gilt-edged AAA rating from all three major rating agencies, the country's debt markets have attracted a solid \$73 billion of net foreign inflow in the past twelve months as well.

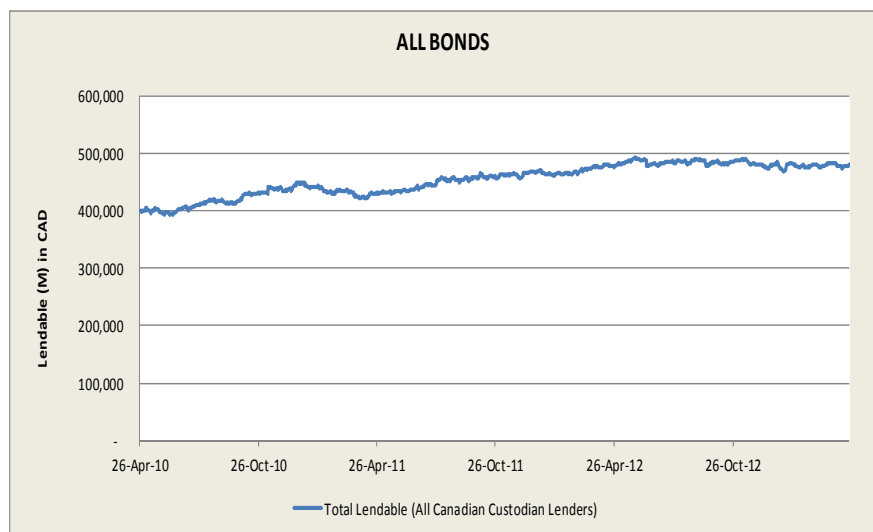
David Rosenberg, Chief Economist & Strategist
Gluskin Sheff + Associates, April 2013

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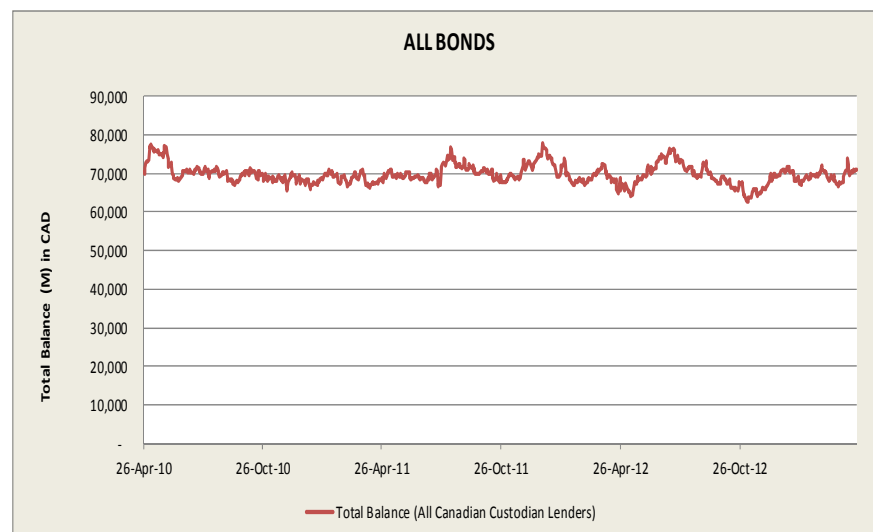
SECURITIES LENDING – FIXED INCOME

- Since April 2010 total market value of lendable bonds (CDN Custodians) increased \$80B CAD or 20%. (480B)
- Total balances since 2010 have ranged between \$63B cad- \$78B CAD.

Total Lendable



Total Balances



Average Balances

2011 - 69,860 (M)

2012 - 69,323 (M)

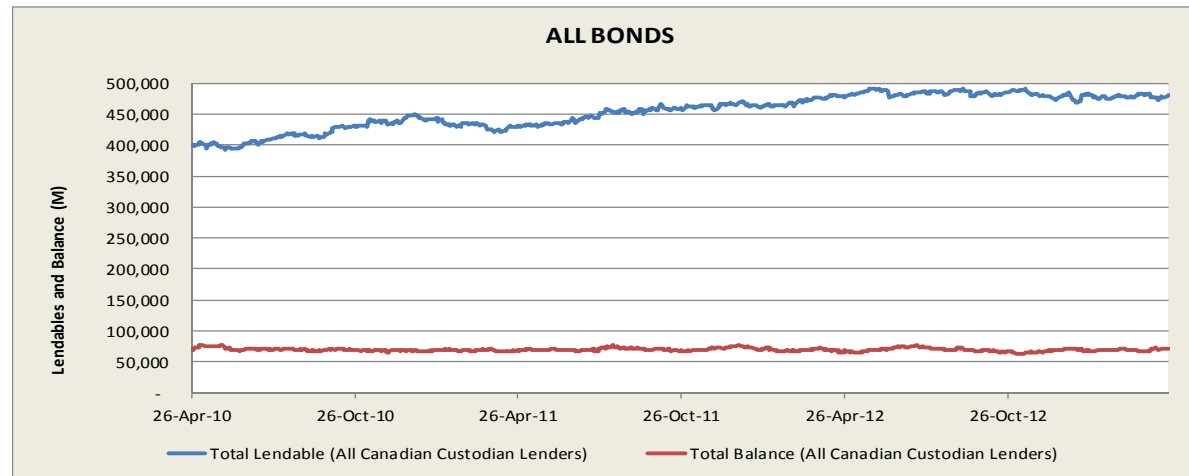
2013 - 69,519 (M)

Data from Performance Explorer

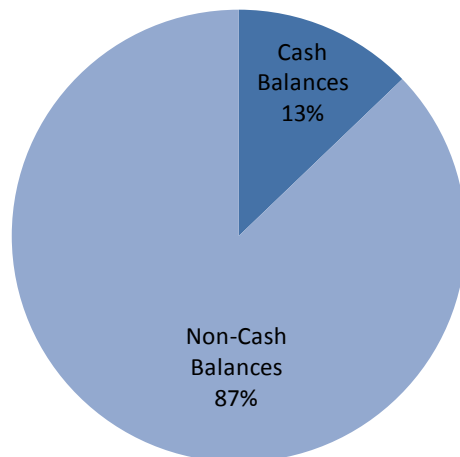
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SECURITIES LENDING – FIXED INCOME

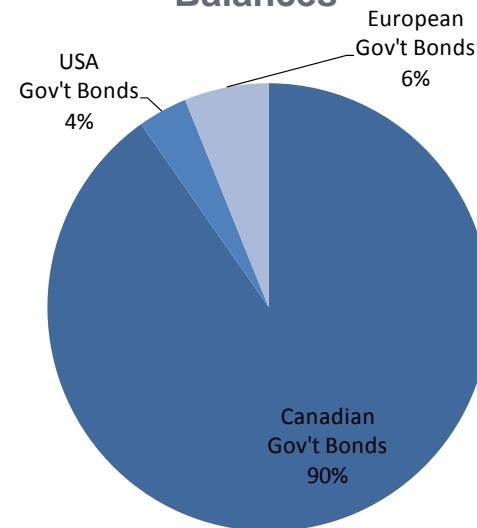
Total Lendable vs. Total Balances



Non-Cash Balances vs. Cash Balances



Government Bond Balances



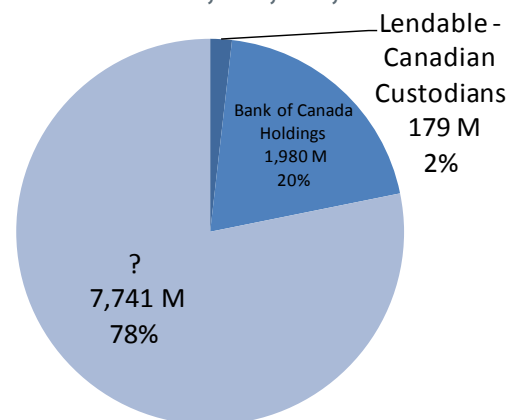
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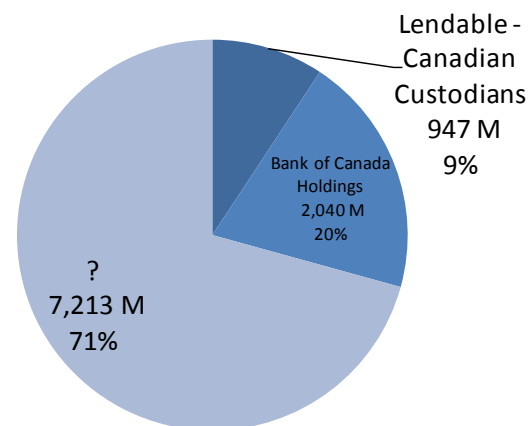
WHERE ARE ALL THE GOVERNMENT OF CANADA BONDS?

S&P – AAA Rating	Outlook
Australia	Stable
Canada	Stable
Denmark	Stable
Finland	Stable
Germany	Stable
Hong Kong	Stable
Liechtenstein	Stable
Luxembourg	Stable
Netherlands	Negative
Norway	Stable
Singapore	Stable
Sweden	Stable
Switzerland	Stable
United Kingdom	Negative

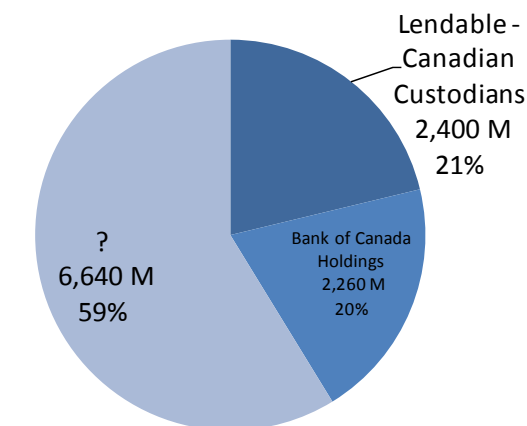
2 yr Gov't of Canada
1.00% 05/01/2015
Total Float 9,900,000,000



5 yr Gov't of Canada
1.25% 03/01/2018
Total Float 10,200,000,000



10 yr Gov't of Canada
1.5% 06/01/2023
Total Float 11,300,000,000



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2013 Major Themes in the Global Fixed Income Markets

- ▶ Rates remain at historically low levels with little prospect of rising significantly in the near future
- ▶ The events of 2007 to 2009 have resulted in lower leverage and a consolidation of market participants
- ▶ Central Banks continue to intervene in an effort to stimulate growth
- ▶ The market is faced with a broad spectrum of regulatory initiatives which place numerous constraints on the secured financing markets
- ▶ Derivative contracts which formally traded over the counter are now required to be cleared via an exchange or central counterparty
- ▶ The use of CCP's is transforming the secured finance markets



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The crisis also highlighted the importance of one type of FMI (Financial Market Infrastructures) in particular- central counterparties (CCPs). A CCP acts as a buyer to every seller and a seller to every buyer for the financial transactions that it clears. An appropriately risk-controlled CCP improves the market's resilience by reducing counterparty credit risk and, therefore, the potential for disruptions to be transmitted through the financial system. This helps essential markets to remain continuously open, even in times of severe stress. A CCP also provides enhanced netting efficiencies to its members, and helps to manage defaults in a controlled manner.

Agathe Cote, Deputy Governor of the Bank of Canada
“Toward a Stronger Financial Market Infrastructure for Canada: Taking Stock”, March 2013