

Operations comment: Pirum



Rupert Perry of Pirum Systems outlines the next generation of post-trade automation - real-time

processing.

Not many years ago, post trade processes in the international securities lending market were mostly manual and often very time consuming. Today, many of the more straightforward operational processes, such as contract comparison and billing comparison, benefit from extensive automation. This allows higher volumes to be processed with much tighter risk control.

But the job of automating all post trade activity is not yet complete, as many other processes are still very manually intensive and require careful coordination and communication between borrower and lender. A couple of good examples are the daily mark to market and returns processes, but there are many others too.

So, why have these processes generally not benefited from automation already? Whereas contract and billing comparison are based on daily/monthly data feeds generated by overnight batch processing, the nature of processes like marks and returns is that they require much more up-to-date data to work effectively and this ultimately requires real time feeds and real time reconciliations, which are more complex and have not been available until more recently.

Furthermore, to successfully automate marks and returns, you first need to have clean and matching positions within contract compare, as there will otherwise be too many exceptions requiring manual processing. It is only within the last few years that most market participants have got on board with this first essential step.

While automated marks in the US Domestic market are usually processed

as part of an overnight batch, this straight forward approach is not viable for the International market, as the required data is simply not available overnight. Marking international securities in Europe (as per ISLA's best practice guidance) requires market participants to use same day closing prices for Asian markets and previous day closing prices for European and North American markets. In Europe, this generally dictates that marks must be processed early in the afternoon, once the closing prices for Asia for the same day are available.

Unfortunately, the requirement to process marks in the middle of the business day creates a new issue relating to timing differences. It is very difficult to find a consistent time during the business day when the timings of each party's internal updates to settlements of new loans and returns, market prices and foreign exchange rates are in synch with each other. If marks are generated and processed when the data is not in synch, this tends to cause a large number of mismatching marks which require further manual investigation/processing.

Using real time feeds to update a set of proposed marks for both parties is a much better approach, as it is more tolerant of the daily variances in the timings of settlement updates or problems that can occur with market data feeds. With real time reconciliation, market participants can immediately identify differences requiring investigation or more simply, if more time is needed for the updates to flow through from the underlying systems. When the marks are ready and in synch, they are automatically posted by both parties in their own books and records.

Today's returns process is another good example of a post trade process which currently requires considerable manual effort from both the borrower and lender to be processed. While borrowers will usually have internal automation to identify when a loan is ready to be returned, they usually need

to call in the returns to the lender by e-mail, fax or telephone call. When the lender receives this request, it has to identify the correct trade(s) and book the required returns in their system.

Using real time data feeds, the complete process of calling in returns can be fully automated, happening within minutes of the borrower booking the return in their own system. Validation logic is applied centrally, before returns even reach the lender, so that any which fail to meet the lender's pre-defined validation criteria can either be rejected immediately or else held in a queue for manual review.

A real time version of contract compare is an essential part of this process, as it automatically determines the correct translation between specific borrower and lender trades in each security, so that when a return is booked by the borrower it is always booked against the correct transaction on the lender's side. This avoids the common contract compare breaks that often result from returns being booked against a different trade in the same security than was intended by the borrower.

As the industry moves forward, it is increasingly apparent that further automation of post trade processes will increasingly rely on real time feeds. It provides both parties with a continuously updating view of the matching state of the transactions in their respective books and records throughout the business day. Real time processing also enables any corrections identified on the reconciliations to be entered in source systems and then fed through to update and correct the reconciliation, ensuring that exceptions are minimised and STP is maximised.



About the author: Rupert Perry is a founding director of Pirum, the leading provider of post-trade automation services to the international securities lending and repo markets. Services provide include real time processing for contract comparison, marks, returns, prepay and exposure reconciliation.