

Securities Lending

The last bastion of manual intervention in an automated trading world

The Topic:

When it comes to securities lending, many funds face similar challenges:

- Without a basis for comparison, the current market rates on borrowed securities often remain a mystery
- The primary focus on short sale execution means profits lost by receiving lower rebates are often overlooked
- Traders often have no choice other than to accept the allocations given to them by their prime brokers.

Viable techniques to more efficiently manage your fund's securities lending business:

- Monitoring rebate rates received on short positions
- Sourcing new securities unavailable at the prime broker
- Increasing income by lending long positions
- Maintain hard-to-borrow positions by reducing potential buy-ins

The Recap of the Luncheon:

The HFBOA luncheon was hosted on Thursday January 14th by Hedge Source LLC and dealt with issues and opportunities available to fund managers with respect to securities borrowing and lending. The presentation was lead by Allen Wolkow, the CEO of Hedge Source along with Janah Angelou, the COO.

It was noted that prime brokerage revenue from just the top players in the field collectively account for over \$ 10 billion per year. The securities lending portion of this total represents a highly profitable area for these firms, and understandably, revenue that they would love to preserve. However, from the fund manager's perspective, examining their securities lending arrangements is a ripe opportunity for capturing additional revenue, lowering costs and gaining better information.

The areas where managers often "leave money on the table" include:

- Short rebates received from prime brokers are not being questioned nor negotiated
- Opportunities to receive income by lending a long security are often missed

Further ongoing issues that managers need help with include:

- Sourcing of hard-to-borrow securities beyond their prime brokerage relationships
- Maintaining a position in a hard-to-borrow security with mitigation of buy-in risk or unannounced adverse changes in a negative rebate rate

The major challenge for managers is that their prime brokers have no vested interest (in fact a disincentive) to provide transparency into their pricing or sourcing of securities. This challenge is exacerbated for firms smaller in scale who are not "prime clients" of the prime broker. There is presently no central clearinghouse for matching those willing to lend securities with those looking to borrow. Hedge Source looks to fill part of that gap by using their own industry contacts and daily sourcing to give an information edge to

fund clients. In addition to the information, they will actively intervene with a client's prime brokers to monitor the rebates received on shorts and to source hard-to-borrow securities that a PB may steer to a more favored client. They will also help to capture revenue on lending securities that a manager is holding long, which often overlooked as an opportunity by fund managers. Hedge Source will provide their services on either a flat-fee or percentage of profit/savings arrangement.

Allen had encouraged all hedge fund managers to actively monitor and negotiate with their prime brokers to capture more of the spread between what's being shared between the parties. He also advised that a manager pick its fights; rather than haggling over all securities, to focus on the ones that are in most demand, and thus the larger reward.

All in all, hedge funds should pay more attention to better monetizing their short and long positions. Certainly this is worthwhile in all markets, but particularly so in a time of challenging returns.

Matt Jenal

More Information:

<http://www.hedge-source.com/>

Presenters:

Allen Wolkow, CEO
HEDGE SOURCE, LLC

Mr. Wolkow has over 35 years of experience in the financial industry. He has worked for major Brokerage Firms as well as spending the last 23 years as a managing director with two Hedge Funds, specializing in Securities Lending. In 1985, while at Lipper & Company he created and managed a multi-billion dollar Securities Lending Department. There he established the initial prototype for Securities Lending Departments for "non self-clearing" investment management firms. In 2002 he replicated that formula and created a Securities Lending Department at Ramius Capital Group LLC. Prior to that, Mr. Wolkow was a General Partner in charge of Options at Janney Montgomery Scott. His background also includes experience in retail sales & brokerage operations. He received a B.A. in Economics from Brooklyn College and served in the U.S. Marine Corps Reserve for 5 years.

Janah Angelou, COO
HEDGE SOURCE, LLC

Ms. Angelou has 15 years of Securities Lending experience serving Hedge Funds and working as a liaison to their Prime Brokers. Prior to forming Hedge Source, Ms. Angelou was a Vice President at Ramius Capital Group, LLC, a multi strategy Hedge Fund headquartered in New York City. At Ramius, she directly serviced the various funds, primarily focusing on PIPES, hard to borrows, and ETFs. Additionally, she helped run a billion dollar conduit book. Prior to joining Ramius, Ms. Angelou worked in the Securities Lending Dept of Lipper Convertibles, LLC, also a multi strategy Hedge Fund, where she worked closely with the traders, sourcing and monitoring

their borrows. Ms. Angelou holds a BA in Communications from the University of Massachusetts, Amherst.