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Securities Lending Yearbook
2009-10

dataexplorers

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Foreword

Welcome to the Securities Lending Yearbook 2009-10, a unique publication that has taken its place in the securities financing industry's calendar as an important, quantitative-led, review of the past 12 months as well as a look ahead to the year to come.

In January last year we commented that 2009 was likely to be a rollercoaster year but actually it has proved to be a year in which the securities financing industry took stock (no pun intended), reduced spending and kept their head down. Thankfully there was no big hitting industry change such as those we saw in 2008 but it also resulted in revenues being a long way from the boom years of 2007 and 2008.

The reduction in volume and activity was probably not unexpected given that the Hedge Fund community started the year in a state of flux with poor performance and mass redemptions. That situation improved as the year progressed and by the second half of 2009 performance was good and money was returning to the hedge funds. Of course with rising equity markets, chances to take negative views on individual names was reduced but we expect to see 2010 offer more opportunities, particularly for those with a view on a W-style recovery.

The themes that are consistent in this year's Yearbook are as follows:

- Increased fees have been earned for hard-to-borrow securities
- Reduced utilisations as we have experienced the decline in general collateral lending
- Reduced cash reinvestment returns

The demand dynamic was broadly matched by the supply side – the beneficial owners spooked by the events at the tail end of 2008 took a while to come back into the market but by the end of 2009 there were signs of returning lenders – the returns are still important particularly amongst a group of Pension Funds who are still, despite the rising markets, affected by under funding issues.

Focus was definitely on regulation in 2009 and this will continue in 2010. It seems that the broad regulatory consensus is that securities lending remains "a good thing". Despite everything you may have read short selling isn't the devil incarnate either – it still is an important tool and regulators gradually lifted any remaining bans during the year but the industry awaits the future of the disclosure regimes across world markets – we continue to hope for a consistent approach but only time will tell if regulators act together.

So what about continued engagement with some of the key commentators on the securities financing business – politicians, regulators and media? We specifically addressed these points at our London and New York events where PR consultants encouraged the industry to continue to push hard at lobbying efforts. It is true to say that the industry associations have stepped up their game in 2009, even if they haven't had quite as many high profile television appearances during the last 12 months. We are pleased to once again feature some viewpoints from these associations in this publication.

We are especially pleased to welcome Deloitte as a partner for this Yearbook for the first time. Their tax perspectives and updates add an important piece of colour to our industry and represent an example of how we seek to improve the outputs in the Yearbook each year.

We also have introduced an update on Brazil for the first time. With investment focus on the BRIC countries, Brazil is the first to develop a significant securities lending and borrowing programme. We hope in years to come to add Russia, India and China but for the moment we are delighted to be able to offer some perspective on Brazil.

We would like to, once again, thank our sponsors who have contributed to the commentaries in the Securities Lending Yearbook 2009-10. Many have been working with us since the inception of the Yearbook over a lunch discussion back in late 2006. If you have picked up a copy of this publication at a conference then thank you – please keep it on your desk during the year and check if our thoughts on 2010 come true in 12 months time. If you need extra copies then let us know or head to our website or the website of one of our partners and download a soft copy or two.

The Yearbook is just one way in which we provide information on the securities financing industry – please do join us at one (or more) of our Securities Financing Forums in 2010. We will be in Hong Kong in September for the first time, as well as hosting our traditional London, New York and Dubai events. Finally, keep an eye on our Webinars which can be accessed via our website. We host a 45 minute panel discussion every six weeks or so which addresses the issues of the day – we look forward to having you join us.

Data Explorers
January 2010

Data Explorers would like to thank the sponsors of The Securities Lending Yearbook 2009-10.

Contents

Predictability in an unpredictable world.

Depend on us for market insight, flexibility and unwavering commitment to service.

Expertise in securities lending. You face unpredictable markets and must respond to the evolving strategies of your clients and competitors. CIBC Mellon offers you flexibility through innovative thinking, market knowledge and open dialogue. You can depend on us for solid execution, professionalism, and a stable growing supply of lendable assets.

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Americas

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Brazil

Brazil is a niche market for securities lending but has attracted strong returns of up to 25%. Expansion is expected in the first of the BRIC markets to see significant volumes.

Brazil's securities lending activity is an operation in which the Brazilian Clearing and Depository Corporation (CBLC) acts as counterparty and guarantees business. The investors offer securities to borrowers to meet temporary needs, generally for 30 days.

There is huge potential in this market: the volume of transactions in November 2009 grew 163% comparing to November 2008 and the average daily trading reached USD 100mn in about 300 contracts. The main lenders were Brazilian mutual funds (33.71%), individuals (28.1%) and foreign investors (25.8%). Among the borrowers, the mutual funds are most active with 40.87% and foreign investor with 34.13%.

Nevertheless the numbers in 2009 are impressive mainly because the comparison is the year of 2008, which was especially hard due to the financial world crises. The loan stock market in Brazil has suffered and short positions dropped. In June 2008 short positions reached USD 23bn and by December 2008 this number was USD 5bn, a decrease of 78%. The loan stock market had a strong increase in 2009, short positions climbed to USD 14bn in November 2009. The total volume in 2008 was USD 175bn and in 2009 USD 121bn, leading us to expect a strong increase in 2010.

Long/short investment funds have grown in popularity in Brazil with 12 funds opening in 2009 alone. Long/short funds have been popular since 2005 with an increase in new products focused on this strategy which have generally been marketed to the wholesale sector for retail investors. These encompass a strategy to buy a particular security and undertake to sell another ("Short Sellers"). The manager sells stocks that it wishes to short and, as it requires three days to deliver, will go to the market to borrow the security it has sold. It is incorrect to assume that the loan market fosters price falls, because it increases liquidity, corrects distortion and prevents artificial valuations.

Significant Securities

The largest short position in Brazil belongs to the company Vale (Ticker VALE5, mining Company) with a total of USD 1.4bn followed by the Oil company Petrobras PN (non-voting shares) with a short position of USD 1.1bn (excluding ADR short position). These two companies represent 20% of the total short position in the Brazilian Stock market. The other important short positions are for Petrobras ON (voting shares) USD 1.08bn, ItauUnibanco (Bank) USD 1.04bn and Bradesco (Bank) USD 687mn. Therefore most interest is in oil, mining and banks, which are the largest Brazilian companies listed on the stock exchange representing 40% of the Ibovespa index, and they also have the largest traded volume on the Brazilian Stock Exchange.

When considering days to cover – short position divided by the stock average traded volume - the picture changes. The top security in days to cover (short interest) is Eletrobrás (ELET6, Utilities Company) with 18 days, followed by telecom company Telesp (TLPP4) 12 days. The other important companies are: Petrobras ON (PETR3, Oil company) 7 days, ItauUnibanco (ITUB4, Bank) 6.5 days and other utilities company Celesc (CLSC6) 6.4 days.

False Signals

Increases in short sales sometimes send false sell signals. When short sales in the Ibovespa (Brazilian Stock Exchange Index) climbed 100% in four months, from January to April 2009 the Ibovespa added 23% in the next three months. Traders are too bearish and the latest equity rally is the beginning of a new bull market. The market is beginning to tentatively price in the likelihood of an economic recovery.

Table 1 – Investors participation in loan stock market

Lenders		Borrowers	
Mutual Funds	33.71%	Mutual Funds	40.87%
Individuals	28.1%	Foreign Investors	34.13%
Foreign Investors	25.8%	Others	9.52%
Others	7.06%	Individuals	6.07%
Corporations	3.89%	Commercial Banks	5.96%
Commercial Banks	0.84%	Corporations	3.45%
Pension Funds	0.49%	Pension Funds	0%

Investors	Lenders		Borrowers	
	R$ Mi	%	R$ Mi	%
Individuals	64,939.52	28.1	14,249.22	6.07
Foreign Investors	59,621.15	25.8	80,110.35	34.13
Mutual Funds	77,918.28	33.71	95,922.29	40.87
Corporations	8,988.32	3.89	8,087.31	3.45
Pension Funds	1,123.95	0.49	9.62	0
Commercial Banks	1,942.24	0.84	13,984.84	5.96
Others	16,580.15	7.06	22,349.78	9.52

Source: CBLC

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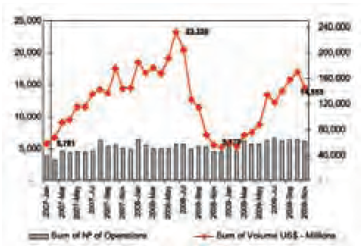
Graph 1 shows the evolution of lent position in terms of volume and number of trades in 2009

Table 2 shows top 10 Brazilian stocks in terms of short interest ratio (number of stocks borrowed / traded volume) in 2009

Table 3 shows the companies with largest open position in USD, they are the largest Brazilian companies, and they also have the largest traded volume in Brazilian Stock Exchange – BM&F Bovespa.

Graph 1
Brazilian Loan stock Market - Evolution



Source: CBLC and Santander Investments.

Table 2
Top 10 Days to cover in 2009 - Median

Ticker	Days to cover Short Interest ratio Median 2009
ELET6	18.28
TLPP4	12.39
PETR3	7.04
ITUB4	6.53
CLSC6	6.47
CSMG3	6.44
GETI4	6.05
CMIG4	5.87
MRVE3	5.83
TNLP4	5.72

Source: CBLC and Santander Investments.

Table 3
Top 10 Stocks in terms of Open Loan Position – December 2009.

Ticker	Short interest Open Loan Position USD
VALE5	1,444,472,114
PETR4	1,183,244,933
PETR3	1,084,623,305
ITUB4	1,043,488,051
BBDC4	686,968,249
GGBR4	541,379,209
VALE3	503,882,041
ELET6	443,278,385
USIM5	355,249,119
CMIG4	320,369,272

Source: CBLC and Santander Investments.

General
In Brazil, the securities lending activities are governed and regulated by Brazilian Securities Commission (CVM – Brazilian equivalent to US SEC) and by Brazilian Monetary Council (CMN). Under Brazilian legislation, there is no specific law designed to address the taxation of securities lending arrangements. However, guidance in respect to the taxation of such transactions is provided through an administrative ordinance issued by Brazilian Inland Revenue (Receita Federal do Brasil - RFB), namely, "Instrução Normativa RFB 742/2007".

Brazilian direct tax considerations
The Brazilian tax treatment of securities lending arrangements depends on where the lender / borrower is resident or domiciled:
lender / borrower resident or domiciled in Brazil: lending fees and interest income on cash collateral is taxed at regressive rates branding from 15% to 22.5% depending on the period of the securities lending arrangement; non-Brazilian lender / borrower that are not resident or domiciled in low tax jurisdictions in accordance to the Brazilian law: For non residents not resident in a 'low tax jurisdiction' (i.e. are those locations or dependencies which impose no income tax, or the existing income tax rate is lower than 20%), lending fees and interest on cash collateral would be taxed at 15%; and other non-Brazilian lender / borrower that are located in a low tax jurisdiction: There is some uncertainty in the market place around the treatment of lending fees and interest on cash collateral, and these are either taxed at 25% or at the regressive rates applicable to Brazilian resident borrower/lenders. In all cases, dividends received by the lender are exempt.

In most cases, securities lending arrangements do not result in a disposition of the lent securities, and accordingly, there should be no capital gains implications on the loan and return of the securities. However, where a financial settlement occurs due to non-return of securities, capital gains would arise for the lender on the difference between the cash received and the average acquisition cost of the security.

Other taxes and considerations
Although no indirect or transfer tax apply to security lending arrangements, non resident lenders / borrowers may be aware of IOF tax, which is imposed at 0.38% whenever a foreign exchange transaction takes place in Brazil (e.g. translation of UDS into Brazilian Reals – BRL).

Based on information current as at 1 January 2010

Deloitte.

Santander Global Banking & Markets Brazil

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Canada

2009 was a year of steady recovery for Canadian securities lending and for the broader Canadian markets, though certainly not to the levels of 2008.

In Canadian equity markets, the S&P/TSX composite index recovered some of 2008's losses, beginning the year at 8,637 and closing at 11,746 for a gain of 36%. The index hit a low of 7,566 on March 9 and a high of 11,779 on December 2.Total financings raised were USD 60bn, which surpassed the previous record of USD 47.6bn set in 2007. 2009 saw a record trading volume of 118.5bn shares, exceeding the record of 109.2bn set in 2008. A new record for transactions was also set in 2009; 191.3mn trades occurred in 2009 compared to the previous record of 182.9mn, which was set in 2008.

In currency markets, Canadian dollar trended stronger following the flight to the USD during the events of fall 2008. Throughout 2009 CAD improved versus much of the G10 including 16% appreciation to JPY, 14% to USD, and 12% to EUR.

Canadian mergers and acquisitions (M&A) deal volume fell according to KPMG Corporate Finance, with 2,110 completed deals valued at USD 129bn. Two bright spots were mining and minerals and oil and gas. The biggest deals of the year included the Petro-Canada/Suncor merger in August and November's spin-off of Cenovus Energy Inc. by EnCana Corporation.

From a tax perspective, the elimination in February of withholding tax on arm's-length interest payments from Canadian residents to US residents was welcome news, paving he way for increased cross-border cash collateral lending.

In regulatory news, in April 2009 CIBC Mellon, RBC Dexia, Northern Trust and State Street Corporation – representing 90% of Canada's securities lending market – founded the Canadian Securities Lending Association (CASLA). CASLA's mandate is to enhance the public's understanding of securities lending in Canada, to encourage the adoption of best practices and to work with regulators and other industry associations to ensure an efficient and secure marketplace.

In September EquiLend announced that it had obtained regulatory approval as an alternative trading system (ATS) in Ontario.

In lending, equity loan balances increased by almost 50% during the year, from USD 23.4bn to USD 34.7bn. Lendable assets increased 57% from USD 225bn to USD 350bn. Equity returns were bolstered by the addition of dividend reinvestment programs for big names such as Bank of Montreal and Canadian Imperial Bank of Commerce. Equity lending revenues took a hit in June when Canadian Oilsands announced the suspension of its premium distribution, distribution reinvestment program and optional unit purchase plan. In August Manulife Financial cut its dividend in half.

Government bonds shorter than 2019 were in high demand and provided lenders with a steady revenue stream in the non-cash environment. Demand for Government of Canada debt collateralised with cash was more evenly distributed to all maturities. Lenders who accepted both types of collateral were rewarded with better balances and bigger spreads.

Graph 1 - Canada Equity

Graph 2 - Canada Equity

Graph 3 - Canada Government Bonds

Graph 4 - Canada Government Bonds

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Canada Equity	352,825.90	59,100.20	8.99	33.14	3.43	4.18
Canada Equity (TSX60)	254,098.20	39,356.10	7.68	23.97	2.40	3.17
Canada Equity (TSX Midcap)	64,169.60	16,128.20	14.98	37.66	6.02	6.72
Canada Equity (Others)	34,558.10	3,615.90	7.52	113.64	7.35	8.09
Canada Government Bonds	225,631.60	54,235.10	25.35	6.41	1.34	3.72
Canada Govt Bonds (Domestic)	114,989.70	40,971.00	35.78	6.11	1.70	4.99
Canada Govt Bonds (International)	2,073.10	207.70	8.89	14.24	1.47	3.62

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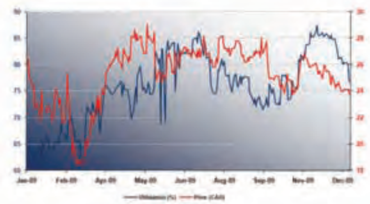
The reinvestment year ended with a much more positive tone than it began, with no liquidity issues this December and spreads continuing to compress. Asset-backed commercial paper (ABCP) conduits continued to amortize as structured, and with virtually no new assets entering the conduits, commercial paper outstanding declined for almost every ABCP program across the country. The Bank of Canada lowered interest rates by a further 125bp in 2009, leaving the overnight rate at a record low of 0.25%. Rates are expected to remain unchanged until at least mid-2010.

Graph 5 - Security of the Year Ritchie Bros. Auctioneers Inc

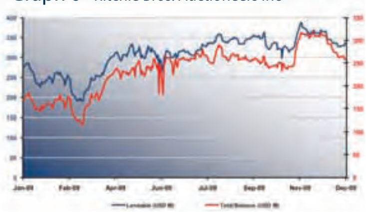


Security of the Year

There was no clear security of the year in 2009. The top ten list by total daily return is dominated by large cap equities with attractive dividend reinvestment programs, including Manulife Financial, Toronto Dominion Bank, Royal Bank and Transcanada Corp.

Our choice for security of the year is Ritchie Bros Auctioneering. A directional short, Ritchie Bros exhibited strong demand through the year, with average utilizations of 75% and average fees of more than 200bp. The stock hit a low of CAD 18.42 on March 2 and a high of CAD 29 on May 19.

Graph 6 - Ritchie Bros. Auctioneers Inc



General

The Canadian Income Tax Act contains rules governing the tax treatment of securities lending arrangements ("SLA"). Arrangements that would be considered securities lending commercially, as well as repos and reverse repos, will generally be SLA's for tax purposes, if entered into between arm's length parties. Certain lending arrangements between non-arm's length persons will also be SLA's.

Canadian direct tax considerations

Payments made to a non-resident of Canada under an SLA may be subject to withholding tax at 25% (this rate may be reduced under an applicable double tax treaty). Lending fees paid to a non-resident lender are treated as interest and should not be subject to withholding tax if paid to an arm's length person. Compensating payments paid to a non-resident lender will either be treated as interest or retain the original character of the income from the borrowed security (e.g., dividends on a share) depending upon the legal nature of the borrowed security and the extent of the collateralization of the loan. Any interest earned by a non-resident borrower in respect of the collateral on an SLA should not be subject to withholding tax.

Where the borrower/lender is a resident of Canada, the deductibility of the compensating payments and the treatment of compensating payments will be determined under general concepts.

The SLA rules deem the lender to not have disposed of the security and to continue to be the owner for tax purposes, thus no capital gains tax implications would apply on the transfer of the security. However, the Act is silent regarding the borrower – so first principles apply – and legally a securities loan is a disposition so the borrower would also be considered to own the borrowed security for tax purposes. For a securities lending arrangement that is not an SLA, the borrower would be considered to have disposed of the security for tax purposes and reacquired it later – and thus could realize a gain or loss on the initial borrowing.

Other taxes and considerations

No indirect or transfer taxes should apply to securities lending arrangements.

Based on information current as at 1 January 2010

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Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Thomson Reuters Corp	CA Equity (TSX60)
2	Manulife Financial Corp	CA Equity (TSX60)
3	Ritchie Bros. Auctioneers Inc	CA Equity (Others)
4	Toronto Dominion Bank	CA Equity (TSX60)
5	Pacific Rubiales Energy Corp	CA Equity (Others)
6	Royal Bank Of Canada	CA Equity (TSX60)
7	Transcanada Corp	CA Equity (TSX60)
8	Sun Life Financial Inc	CA Equity (TSX60)
9	Bank Of Nova Scotia	CA Equity (TSX60)
10	Bank Of Montreal	CA Equity (TSX60)

Graph 7 - Ritchie Bros. Auctioneers Inc

All graphs and tables have been sourced using the Data Explorers suite of products.

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US Equities

The US equity lending market remains the largest in the world. At USD 320bn at year end it represented 48% of global equity lending and comfortably exceeds the European equity lending market combined (USD 160bn) and dwarfed the combined Asian equity lending market (USD 33bn).

As with many markets the US equity market lendable assets rose during the year (the currency impact was neutral) to end at USD 3.155tn as graph 1 illustrates. The borrowing of securities increased in absolute terms from USD 270bn to USD 320bn but utilisation dropped year on year from 11.49% to 9.69%. Overall fees rose just over 5bp to average 67.83bp.

Market Analysis

However, as is so often the case and as clearly demonstrated by graph 2, the averages displayed in table 1 only tell a partial story. Lending fees for the smaller capitalisation securities have fallen by about 50% year on year but S&P 500 lending fees have risen from an average of 33bp to 75bp. The TRTL for the S&P 500 has risen from 4.7bp last year to 7.32bp. The increase comes predominantly from lending fees rather than reinvestment returns which have remained static at about 2bp. This possibly indicates that a movement towards intrinsic value lending at the appropriate fee rather than the historic dependency upon cash re-investment has occurred (71% this year compared to 44% last year of average TRTL came from SL fees orthat lending Citigroup skewed the whole S&P 500 market - more of which later).

Significant Securities

Citigroup, General Motors and Ford return from the 2009 top ten in the S&P 500. Under Armour, Sunpower and NetFlix reappear in the Russell 2000 and Chipotle Mexican Grill is the sole representative making a repeat appearance in the smaller capitalisation class. This relatively high turnover of names year on year marks the US market out as quite unusual. The US market is a large mature market and exhibits many characteristics of being such. The liquidity, depth and breadth of the securities lending market is one of the many contributory factors that goes towards ensuring an efficient market.

Security of the Year

Seldom do you see a market, let alone a global activity, so dominated by one security as we did in 2009. Citigroup is without doubt the security of the year in the US and globally. The annual average fee for lending the shares exceeded 26% and reached weighted average levels of above 80%. Individual trades were done at over 100% at the height of the transaction and this security alone contributed 10% to entire global lending revenues. If you owned and lent Citigroup well in 2009 you had a good year. However, if you didn't, you didn't.

So what was the transaction?

On 27th February 2009 an exchange was announced converting common stock for publicly held convertible and non-convertible preferred shares. The transaction was intended to build Citi's Tangible Common Equity to a level that removed uncertainty and restored confidence in the company. The market reacted to a significant technical opportunity by selling the underlying shares and buying the preferred shares. As a result demand to borrow the ordinary shares rocketed (as did the cost of borrowing).

The spread in the arbitrage was small, so to profit those engaged had to do the trade in large scale. The conversion at the end of the transaction occurred and Citi quickly returned to its prior status as a general collateral security in the lending market.

The transaction raised many interesting issues which are relevant to the broader market. It highlighted the extent to which borrowing and shorting of securities can be driven by arbitrage and the need for a hedge rather than a directional bearish view. It opened up a healthy debate about the allocation of returns within the overall capital markets. Some traders felt the lenders were being too greedy and decided to boycott the transaction.

Outlook

The US securities lending market is a central part of the largest capital market on earth. The outlook from the market is for one that will focus more on intrinsic lending at the appropriate fee rather than depending upon cash re-investment and the leveraging of difficult to borrow securities into large balances of easy to borrow securities. Inter broker lending and "box" lending of margin and fully paid for securities will continue to increase in importance. The embryonic moves to exchange traded securities lending will probably take hold in the US before they do so anywhere else – time will tell. Against such a backdrop the market waits to see what the SEC will do. Doing nothing does not seem to be a likely option and whatever they change it will have ramifications for the US and other markets.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
USA Equity	3,155,104.40	320,310.20	9.69	67.83	6.39	9.31
USA Equity (S&P500)	2,396,087.80	161,853.10	6.88	75.30	5.23	7.32
USA Equity (Russell 2000)	300,901.10	68,619.20	21.20	63.69	13.13	19.43
USA Equity (Others)	458,115.60	89,837.90	17.45	46.74	8.18	13.37

Table 2 - Security Rankings by Total Daily Return

Rank	S&P 500	Russell 2000	US Equity (Others)
1	Citigroup Inc	Synaptics Inc	Chipotle Mexican Grill Inc
2	Sears Holdings Corp	Under Armour Inc	Factset Research Systems Inc
3	General Motors Corp	Sunpower Corp	Alliance Data Systems Corp
4	American International Group Inc	Netflix Inc	Mead Johnson Nutrition Co
5	M&T Bank Corp	Mannkind Corp	Nordic American Tanker Shipping Ltd
6	Ford Motor Co	First Solar Inc	Mgm Mirage
7	Wynn Resorts Ltd	Buckle Inc	Freddie Mac
8	Merck & Co Inc	Green Mountain Coffee Roasters Inc	Federal National Mortgage Association (Fannie Mae)
9	Fastenal Co	Texas Industries Inc	Barnes & Noble Inc
10	Vulcan Materials Co	Realty Income Corp	Macerich Co

General

Section 1058 of the U.S. Internal Revenue Code specifically deals with the U.S. taxation of securities lending arrangements and states that no gain or loss should be recognized on the transfer of securities in exchange for an obligation under such a lending agreement, subject to the following conditions:

- The borrower must return to the lender securities identical to those originally transferred;
- During the period of the lending arrangement the borrower must make payments to the lender equivalent to any interest, dividends or other distributions that the lender is entitled to (see discussion of tax consequences below);
- The lending agreement must not reduce the risk of loss or opportunity for gain for the lender;
- The arrangements must meet any such future requirements as the U.S. Treasury Secretary may prescribe by regulation.

U.S. tax may arise in the event that securities are transferred under an arrangement that was intended to comply with the requirements of Section 1058 but subsequently failed to do so.

US direct tax considerations

In general, if the borrower is a U.S. person, borrow fees are treated as U.S. source and subject to 30% U.S. withholding tax unless an applicable income tax treaty reduces such withholding to zero under relevant paragraphs concerning 'other income' or business profits'.

Rebate fees, i.e., interest income on cash collateral (deposits) posted with a U.S lender would be subject to 30% U.S. withholding tax unless U.S. domestic law or an applicable income tax treaty reduces such withholding under relevant paragraphs concerning interest.

Substitute payments made to the lender under a securities lending arrangement would retain the character and sourcing of the underlying payments (i.e., treated as interest or dividends depending on the security involved). Therefore, payments made to non-residents with respect to borrowed U.S. securities would be subject to U.S. withholding tax generally at a rate of 30% (or lower if an income tax treaty applies). Please note that Notice 97-66 is currently still applicable to dividend substitute payments made under a typical lending arrangement involving U.S. securities (however; see comments below).

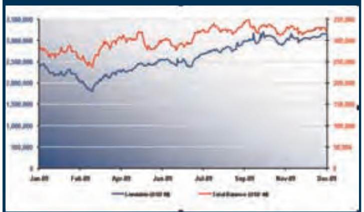
Other taxes and considerations

There is currently no indirect or transfer tax regime in the U.S applicable to securities lending arrangements. In addition, pursuant to the US Senate Permanent Subcommittee on Investigation's report on Dividend Tax Abuse, Notice 97-66 which currently regulates foreign to foreign lending, is to be revoked and replaced by the Foreign Account Compliance Act of 2009 (contained within the Tax Extender Act 2009).

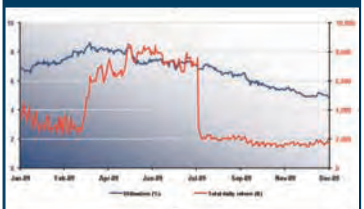
Based on information current as at 1 January 2010

Deloitte.

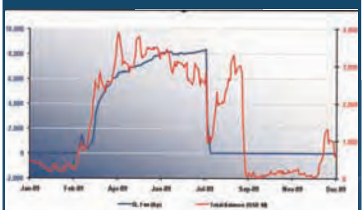
Graph 1 - USA Equity



Graph 2 - US Equity S&P 500



Graph 3 - Security of the Year
Citigroup Inc



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Asia

Pan Asia Securities Lending Association (PASLA) Newsletter 2009

The past year was another challenging year for Asia Pacific's Securities Borrowing and Lending industry. However, with the reduction of counterparty credit and collateral concerns that had defined the Securities Borrowing and Lending landscape in Asia in 2008, and the revival of market indices globally, short selling restrictions introduced around the region since 2008 were largely curtailed.

In the second and third quarter of 2009, funds flow into the Asian equities market steadily improved, and lenders reentered the markets. Between January and December 2009, Asian lendable balances rose from over USD 500bn to approximately USD 700bn in December 2009, a 40% increase. Although still 30% below the lendable balances of December 2007, the improvement in overall market indices, has helped create stronger positive sentiment among institutional lenders.

While the recovery in securities markets is driving healthier lender sentiment, the past year has also brought a greater understanding of the benefits of SBL and short selling. In particular, a greater appreciation among financial regulators of the benefits of short selling and SBL - providing market liquidity, efficient price discovery, facilitating hedging and risk management, reducing settlement risks - has contributed to the reduction of short selling restrictions, and reinvigorated lending activity in the process. In May, the Australian Securities and Investment Commission (ASIC) announced an immediate lifting of the ban on covered short selling of all financial stocks listed on the Australian Stock Exchange. Subsequently, the Korea's Financial Services Commission (FSC) lifted the covered short selling ban on all stocks except for financial securities listed on the Korean Stock Exchange (KRX). The ban on financial stocks continue to this day, but represent the exception to the general lifting of short selling bans around the region.

The lifting of short selling bans in Australia and Korea were also supported by additional moves by other Asian regulators and exchanges to promote the development of securities lending. In August 2009, the Bursa Malaysia announced the introduction of the SBL Negotiated Transaction (NT) model – an enhanced version of the existing SBL Central Lending Agency (CLA) model, - which is very similar to structures already introduced into both South Korea and Taiwan. This change is expected to allow international lenders to participate in Malaysia's SBL market in 2010.

Central to our objective as the primary industry body for the Asia Pacific Securities Borrowing and Lending industry, PASLA worked closely with both industry participants and regulators on securities lending and borrowing regulations, buy-in practices and measures to provide greater transparency. Key highlights of PASLA initiatives are summarized below.

Throughout the challenging market conditions, PASLA, International Securities Lending Association (ISLA), London Investment Banking Association (LIBA), Securities Industry and Financial Markets Association (SIFMA) and Risk Management Association (RMA) have been in regular discussion with respective financial regulators. In May 2009, we made a joint representation to the International Organization of Securities Commissions (IOSCO), in support of 'short selling within a well-structured regulatory framework' and a more consistent regulatory approach internationally. This followed a joint press statement issued with ISLA, RMA, SIFMA and ASLA in September 2008 and the working group discussions with SIFMA and ISLA in December 2008.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Asian Equities	680,168.90	63,476.70	76.91	8.55	5.74	7.14
Australia Equities	157,703.20	14,049.40	9.44	46.11	4.16	5.29
Hong Kong Equities	139,819.30	15,081.10	11.56	99.75	11.09	13.03
Japan Equities	293,106.40	27,167.80	7.84	67.06	4.19	5.65
South Korea Equities	40,355.30	2,031.90	4.69	152.98	8.92	9.58
Singapore Equities	33,740.90	3,747.40	9.95	91.67	8.41	9.82
Taiwan Equities	6,888.50	1,230.30	0.14	348.65	0.52	0.52
Thailand Equities	3,949.50	77.30	2.32	169.01	3.64	3.78
New Zealand Equities	1,778.40	83.60	6.41	84.90	4.10	4.83
Indonesia Equities	624.70	0	0.21	321.76	0.65	0.65
Malaysia Equities	1,148.20	0	0.17	350.00	0.61	0.61
Philippines Equities	553.20	7.80	1.25	362.00	4.53	4.53
China Equities	501.30	0	0.32	87.47	0.42	0.43

The move towards greater transparency in the reporting process for securities lending, essentially an over-the-counter activity, was also a primary focus for PASLA in 2009. The Australian Securities and Investment Commission (ASIC) issued a consultation paper on Securities Lending and Substantial Holdings Disclosure in July 2009, which specified proposals to improve the disclosure of substantial holdings in practice and included securities lending and prime broking arrangements when calculating a substantial holding. In August 2009, the Australian Securities Lending Association (ASLA), together with PASLA, ISLA and RMA, submitted a letter to support the objectives of the substantial holdings provisions and propose that ASIC grant relief to securities lending participants, to alleviate multiple reporting of relevant interests in the same securities by different participants. This occurs by allowing intermediaries to hold only net positions in calculations for Substantial Shareholding Notifications (SSN) and by allowing lenders to include either on-loan or collateral positions, but not both, in calculations for SSNs. Additionally, this process works by not requiring Prime Brokers to include in their own calculations for SSNs, client securities that have not been received but available for loan, for SSN calculation.

The efficiency and feasibility of securities lending settlement processes for industry participants forms a core part of PASLA's representations. PASLA has been in regular dialogue with the Singapore Exchange on enhancements to their settlement systems and timelines. Prior to the launch of the Pre-Settlement Matching System (PSMS) in the second quarter of 2010, the Central Depository (Pte) Ltd in Singapore announced exceptional processing for SBL recall transactions, effective from 14 December 2009 to the second quarter of 2010. This temporary process essentially brought the buy in process forward to midday on T+3, requiring Depository Agents to have sufficient securities in their accounts before 10am on T+3.

Throughout 2009, PASLA has also worked with Asian regulators and exchanges on development of their securities borrowing and lending framework, sharing industry best practices and feedback from participants. In September 2009, as part of the International Securities Finance (ISF) series of master class events, PASLA along with the Securities and Exchange Board of India (SEBI) spoke on the development of SBL within India and other regional markets. PASLA continues to engage SEBI and the Indian exchanges on the ongoing development of India's SBL onshore platform and market.

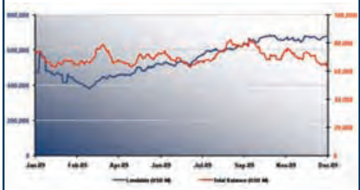
For the first time in 2 years, we start the new year with a sense of expectancy, and the market developments from the first week of the year have not disappointed.

In the first week of 2010, the Monetary Authority in Singapore (MAS) issued a consultation paper on the harmonization of securities lending rules within the various market sectors under their authority, SEBI in India has issued amendments related to the loan tenor and early termination of loans, and the China Securities Regulatory Commission (CSRC) has approved the introduction of margin trading and securities lending, as well as index futures. Pilot testing will be conducted with selected local brokerage firms before these facilities can be widely offered in the market.

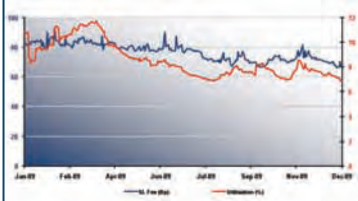
PASLA and the industry members are excited by these announcements, and the association looks forward to the opportunities for new market developments in 2010.

Written by Lawrence Komo, Chairman of PASLA & Asia Pacific Head of Investor Services, Citi

Graph 1- Asian Equities



Graph 2- Asian Equities



All graphs and tables have been sourced using the Data Explorers suite of products.

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Australia

After a tumultuous year in 2008 things calmed down significantly in the Australian market in 2009. Australian regulators are in the vanguard of the process of improving disclosure of both securities lending and short selling.

Market Analysis

One of the few major economies to avoid falling into recession, the Australian market continued to lead the world in the promotion of transparency regarding securities lending and short selling. The investment community faced significant challenges communicating with their trustees and boards. The press remained on the front foot, but improved education, communication and transparency helped stabilise the lending market.

Overall utilisation of the equity market has fallen from over 12% at the start of the year to below 8% at the end. Demand and fees for lending securities remains in line with the previous year, although the continued dependency upon dividend dates is apparent from the spikes in fees and utilisation.

The recovery in asset price value combined with the strength of the AUD versus the USD has driven the value of the lendable inventory in Australian equities up 115% to over USD 157bn from last years close of USD 73bn. Despite, or perhaps because of these drivers, utilisation collapsed to 9.53% from last year's 20.59%. Clearly the prospect of being short securities with price appreciation at such levels was not attractive and the volume of directional shorts reduced dramatically. With securities lending fees remaining stable year on year at 46bp, and the uptick available from cash re-investment being limited, the TRTL halved from last years 11.86bp to this years 5.41bp.

This trend is repeated in all equity classes - irrespective of capitalisation. The picture in Government Bonds is similar.

Australian regulators have responded with vigour to the demand for more transparency in short selling and securities lending. As a result of the regulatory uncertainty many traders have focused their short activities in other markets and it will be interesting to see whether the observed reduced utilisation of assets (which is a commonplace global phenomenon) increases in the future.

Significant Securities

Macquarie Group, our Security of the Year in 2008, topped the return chart in 2009 again but we suspect will fall from this lofty position in 2010 based on its fall in utilisation during the year from levels of 80% to 20%.

Leighton Holdings was a newcomer to the Top 10 in 2008 and we commented on the interest in the company last year which, if anything, intensified in 2009. Utilisation halved from 70% during the first half of the year as the share price doubled but utilisation picked back up to 60% later in 2009.

Rio Tinto, a former Security of the Year, was again in demand when it announced a rights issue in June but otherwise interest was relatively benign.

Other names in the Top 10 were in demand over dividend dates but otherwise activity was slight.

Security of the Year

A newcomer to the Top 10 this year is Fairfax Media which had a combination of events in 2009 that conspired to attract directional interest. Fairfax Media started the year with an asset sale, continued with a credit downgrade and a decision not to pay a final dividend before culminating in a boardroom change with the appointment of a new Chairman. The share price actually moved upwards during this activity, doubling from March to year-end.

Outlook

The Australian securities lending market is less profitable than it was last year. Despite the fact that absolute lending volumes held their ground, the performance of the market combined with the strength of the currency and changes in the regulatory regime have reduced both the profitability of and the propensity to trade on the short side.

There are always dividend related transactions and M&A related transactions to take advantage of but the trader looking for a light regulatory touch may continue to avoid Australia. The implications for market efficiency, price discovery and the development of financial markets are well worth considering and the Australian authorities have placed their market at the centre of this important and ongoing debate.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	**Lendable Assets (USD m)**	**Total Balance (USD m)**	**Utilisation (%)**	**SL Fee (bp)**	**Securities Lending Return to Lendable (bp)**	**Total Return to Lendable (bp)**
Australia Equity	157,703.20	14,049.40	9.53	46.60	4.24	5.41
Australia Equity (ASX MidCap)	16,138.40	2,786.00	15.05	47.30	6.42	8.34
Australia Equity (ASX SmallCap)	10,107.40	1,738.70	15.48	94.71	11.41	13.14
Australia Equity (ASX50)	125,091.30	9,052.00	8.61	39.46	3.51	4.57
Australia Equity (Others)	6,366.10	472.70	5.28	81.60	3.57	4.26
Australia Government Bonds	15,224.40	2,847.90	17.64	5.91	1.09	1.46
Australia Govt Bonds (Domestic)	4,876.50	1,317.20	26.21	7.35	2.01	2.78
Australia State Bonds (Domestic)	10,198.50	1,530.60	13.39	4.13	0.56	0.68

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Macquarie Group Ltd	AU Equity (ASX50)
2	Leighton Holdings Ltd	AU Equity (ASX50)
3	Rio Tinto Ltd	AU Equity (ASX50)
4	National Australia Bank Ltd	AU Equity (ASX50)
5	Westpac Banking Corp	AU Equity (ASX50)
6	Bhp Billiton Ltd	AU Equity (ASX50)
7	Australia And New Zealand Banking Group Ltd	AU Equity (ASX50)
8	Fairfax Media Ltd	AU Equity (ASX50)
9	Commonwealth Bank Of Australia	AU Equity (ASX50)
10	Qbe Insurance Group Ltd	AU Equity (ASX50)

General

Eligible SLAs are specifically dealt with in Australia under section 26BC of the Income Tax Assessment Act 1936. A number of criteria need to be satisfied for section 26BC to apply to the borrower and lender, including a written SLA agreement under which the replacement securities must be provided to the lender less than 12 months after the borrowed securities were borrowed, and any distributions during the payment must be paid to the lender.

Recently introduced provisions dealing with the tax timing of income and deductions for financial arrangements would also require consideration.

Australian direct tax considerations

The effect of section 26BC is to reflect commercial practice, which treats SLAs as loans. Section 26BC allows the lender and borrower to ignore the sale and repurchase of the securities for tax purposes. Accordingly, no taxable gain or loss is deemed to arise on the SLA.

If section 26BC does not apply, the transfer of title to the borrowed securities would usually give rise to a taxable gain or loss for the lender and transfer of title to the replacement securities would usually give rise to a taxable gain or loss for the borrower.

For Australian tax residents borrowers and lenders, and non-residents from a country with which Australia has a tax treaty that engage in SLAs through a permanent establishment in Australia, fees receivable /payable, distributions (or compensatory payments) paid to the lender and interest on cash collateral provided under the SLA would be assessable/deductible under ordinary rules.

Non-residents from a country with which Australia does not have a tax treaty that engage in SLAs would be subject to tax in Australia on lending fees, distributions (or compensatory payments) received or profits from SLAs on revenue account, if the SLA activities have an Australian source.

Interest paid to a non-resident on cash collateral may, however, be subject to interest withholding tax.

Other taxes and considerations

Transfers of securities and collateral under SLAs generally should not be subject to Australian goods and services tax ('GST'). Fees and charges payable, margin calls and refunds and interest on collateral should also not be subject to Australian GST. Certain agency fees, however, may be subject to Australian GST.

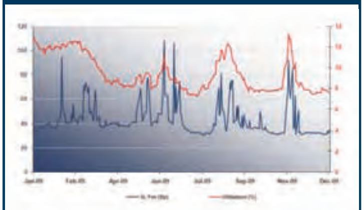
Transfers under SLAs of securities that are listed on an official stock exchange should not be subject to Australian stamp duty. Transfers under SLAs of securities that are not listed on an official stock exchange may give rise to stamp duty if the securities are issued by an entity with a sufficient connection with Australia.

Based on information current as at 1 January 2010

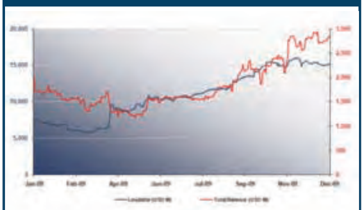
Deloitte.

Graph 1 - Australia Equity

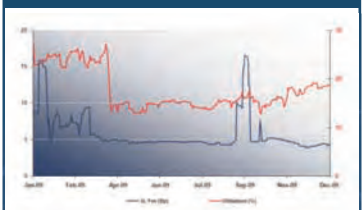
Graph 2 - Australia Equity



Graph 3- Australia Government Bond



Graph 4 - Australia Government Bond



Graph 5 - Security of the Year
Fairfax Media Limited

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Hong Kong

Structural consolidation played heavily as the flight to quality continued throughout the year. Earlier fears were quashed and sentiment improved as the impact of multiple economic stimulus policies gained momentum. The HSI and HSCEI closed the year up 56.65% and 66.06% from a fragile start to the year. The combination of stronger markets in 2H 2009, structural consolidation, equity volatility dropping by more than half and the knock-on effects from the credit crunch resulted in a 36% fall in the daily average short sales volume in Hong Kong*.

During the first half, the knock-on effects from the credit crunch had two distinctly opposing forces: firstly, continued counterparty fears impacted the ability to trade and lines were withdrawn by lenders; secondly, market fears resulted in heightened desires to hedge exposures. The SBL desks that could successfully balance these opposing factors felt a marked pick-up in business volumes at the expense of the broader SBL market. As the market settled and gained momentum in the second half of the year, more positive press relations and communications resulted in lending programmes being restarted and new entrants emerging.

Key highlights from the first half revolved around sectors most affected by the credit crunch, requiring market participants to hedge positions or take directional decisions based on fundamentals. In each sector a particular stock was centrally used as a proxy for the sector:

- Banking Sector: HSBC (5HK)
- Construction Sector: China Railway (390HK)
- Food: Tingy Noodles (322HK)
- Consumer Electronics: BYD Co (1211HK)

Banking IPOs from late 2008 (eg. CCB and Bank of China) drove up demand as we entered 2009 as market participants hedged long positions via a range of derivative products.

During the second half of the year the market gained momentum leading to large increases in Placement Issuance as major shareholders looked to take advantage of a more buoyant environment. These factors drove demand with significant focus around HSBC 5HK which issued rights on their HK, London and US lines as well as being a cross border play for many arbitrage participants.

Securities Lending Influences and Trends

The market experienced a reduction in the amount of Securities Lending participants as the credit crunch increased counterparty fears and short selling received significant negative press. For the larger and more established desks the extent of their longer term relationships dictated whether supply contracted or not.

Since short selling restrictions were imposed in many markets back in 2008, there has been a focus for regulators across the globe to make short selling more transparent; similar discussions are ongoing in Hong Kong. However, it is worthy to note that in Hong Kong, the regulators did not impose short term restrictions and allowed the market to trade freely during this time, which was a testament to the regulatory framework and the levels of short selling transparency already in place.

Other significant influences revolved around the shortage of cash and lenders changing their risk models, taking in less riskier assets after the default event in 2008. Cash collateral was certainly in vogue.

Moving forwards, we expect to see more supply coming on to market and the possibility of short seller transparency. Demand for Hong Kong equities could increase should discussions substantiate around making HK 'H' shares and 'A' shares fungible.

Security of the Year

Security of the Year was Angang Steel. This was one of many Hong Kong equities where borrow demand had diverse drivers:

- The 'A' vs 'H' share arbitrage was popular in the 2H 2009 with borrow levels spiking at a time when availability was squeezed.

- Constant Iron Ore price negotiations which received global press coverage had a big effect on borrow demand.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Hong Kong Equity	139,819.30	15,081.10	11.68	100.33	11.26	13.27
HK Equity (HSI)	88,518.20	7,246.40	10.60	46.74	5.78	7.64
HK Equity (Others)	51,301.10	7,834.70	13.95	165.20	22.92	25.26

*Source: HK Stock Exchange

HSBC

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Industrial And Commercial Bank Of China Ltd	HK Equity (HSI)
2	Bank Of China Ltd	HK Equity (HSI)
3	Angang Steel Co Ltd	HK Equity (Others)
4	Alibaba.Com Ltd	HK Equity (Others)
5	Bank Of Communications Co Ltd	HK Equity (HSI)
6	China Construction Bank Corp	HK Equity (HSI)
7	China Zhongwang Holdings Ltd	HK Equity (Others)
8	China Merchants Bank Co Ltd	HK Equity (Others)
9	Hsbc Holdings Plc	HK Equity (HSI)
10	Byd Co Ltd	HK Equity (Others)

General

Hong Kong domestic legislation provides for an exemption from Hong Kong profits tax for stock borrowing and lending transactions by allowing disposals and reacquisition of "specified securities" (e.g. listed debt or equity securities) under certain stock borrowing and lending agreements to be disregarded for Hong Kong profits tax purposes.

Hong Kong direct tax considerations

Certain conditions must be met for the exemption to apply. Broadly, the borrowed stock under a lending agreement must be used by the borrower for a "specified purpose" (e.g. settling a sale) and stock of the same description must be returned to the lender within a specified period. Further, the lender must be compensated for any distributions received by the borrower. Both the borrower and lender should be dealing with each other at arm's length and the transaction must not be entered into with the purpose of avoiding or deferring amounts which would otherwise be chargeable to Profits tax.

The Hong Kong tax system is based on a territorial concept and not residency. Accordingly, only Hong Kong sourced profits derived from a trade, profession or business in Hong Kong are subject to Profits tax. For borrowers and lenders who are not considered as carrying on business in Hong Kong, no taxes should fall due as a result of lending transactions on lending fees, rebates or manufactured payments. For lenders or borrowers who carry on a business in Hong Kong, the general principle (e.g. based on location of services for lending fees and other specified rules for interests for manufactured payments arising from such distribution) would apply to determine Profits tax. However, the receipt of a dividend distribution by a borrower and manufactured dividends to the lender should be ignored for tax purposes because dividends are generally exempt from tax in Hong Kong.

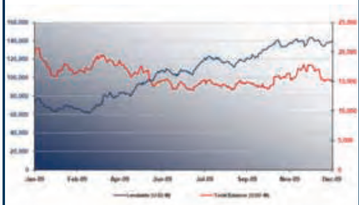
Other taxes and considerations

Where specific conditions are satisfied, stock lending arrangements are not treated as transactions which will give rise to stamp duty. However, it is important to note that this concession only applies to the sale and purchase of Hong Kong stock which is subject to the rules and practices of the Stock Exchange of Hong Kong Limited. In other words, shares in private companies do not fall within the scope of the relief.

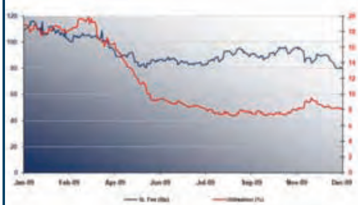
Based on information current as at 1 January 2010

Deloitte.

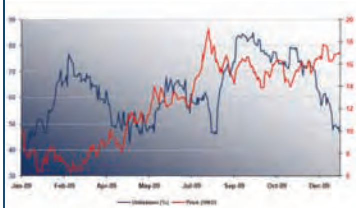
Graph 1 - Hong Kong Equity



Graph 2 - Hong Kong Equity



Graph 3 - Security of the Year
Angang Steel Company Limited



Graph 4 - Angang Steel Company Limited

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Japan

The Japanese securities lending market remains the largest Asian securities lending market with USD 27.16bn of outstanding loans as at year end. This represents a decline of 29% when compared with balances a year previously. The scale of the Japanese market still comfortably exceeds both the Hong Kong and Australian markets which are the second and third largest Asian securities lending markets respectively. At year end Japan represented 42% of the Asian equity balances.

Globally the securities lending industry is smaller this year than it was a year ago and the Japanese market is no exception. Lendable inventory has reduced from USD 372bn at the start of the year to USD 293bn at year end and balances, which started the year at USD 35bn ended it just over USD 27bn. During the April and September reporting periods the balances topped USD 45bn and USD 41 bn.

Market Analysis

Compared to a year ago the Japanese lending market overall is not only smaller than it was, but less profitable. Overall utilisation has fallen from 9.97% to 7.88% and despite an increase in fees from 60.49bp to 67.70bp the total return to lendable fell from 7.85bp to 5.75bp. These headlines mask the fact that lending Nikkei 225 securities was more profitable lending (3.13bp versus 2.84bp) but when one factors in the less lucrative cash re-investment returns the total return to lendable remained lower than last year (4.38bp versus 4.94bp). Outside of the Nikkei 225 the total return to lendable dropped significantly from 15.58bp to 9.69bp.

Graph 1 shows that the averages don't tell the whole picture – far from it. The decline in both absolute daily income and total return to lendable throughout the year is obvious to see.

The Japanese market has exhibited the characteristics of a maturing securities lending market and the benign re-investment environment has not assisted returns.

Significant Securities

Eight of the top ten securities, as rated by average total daily return are drawn from the Nikkei 225 – the exceptions being Acom and Promise. Last year there were 4 smaller cap securities in our top ten. Five companies made this years top 10 and last years : - Resona Holdings; Mitsubishi Motors, Mizuho Financial Group; Japan Airlines and Sumitomo Mitsui Financial Group. The significant challenges faced by the financial, motor and airline industries are longstanding global issues and not unique to Japan.

Mitsubishi Motors was "Security of the Year" last year in the yearbook and has "enjoyed" another high profile year in the lending market. Utilisation has been consistently over 60% and topped 85% on a couple of occasions as the price of the security oscillated from under 120 yen to 180 yen and back again.

Security of the Year

When looking for a security of the year one is looking for a security that has a story to tell and that many readers will identify with and may even have bought, sold, lent or borrowed. This year in Japan the security of the year is Japan Airlines. As the chart shows the utilisation of the security rose to over 70% as the challenges faced by the company refused to go away. The share price performance over the year rewarded those who were short of the stock and declined from over 200 yen to under 70 during the course of the year.

Revenue attribution is always worthwhile considering. As the chart below shows the cost of borrowing Japan Airlines in the wholesale market rose from an historic 400bp to over 600bp in the fall and 100% of the income comes from the intrinsic value associated with lending the security rather than from cash re-investment.

At time of writing JAL has just applied for protection from creditors under the Corporate Rehabilitation Law - Japan's version of Chapter 11 - with the Tokyo District Court. The burden of a USD 25.6bn debt mountain and the difficulties of operating in an increasingly competitive global airline industry meant that shares will be removed from the Tokyo Stock Exchange on Feb. 20, wiping out investors. No one likes to see a company in such difficulties but one has to admire those that took a view and shorted the security at 200 yen or more. They did not cause the company's difficulties but they did profit from them.

Outlook

We would expect 2010 to be a year in which Japan retains its Asian securities lending leadership - although we might see more growth from India and China at the margins – given recent regulatory developments. Clearly, the performance of the overall market and the strength of the Yen will have a significant impact upon lending values – and if we knew in which direction and to what extent we'd be running a macro hedge fund and not working for Data Explorers. The expansion of Japanese Banks in the global capital markets will promote activity and the resurgence of the convertible bond sector will have a positive impact upon securities lending activity.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Japan Equity	293,106.40	27,167.80	7.88	67.70	4.25	5.75
Japan Equity (Nikkei 225)	212,814.30	17,283.70	6.99	58.55	3.13	4.38
Japan Equity (Others)	80,292.10	9,884.00	10.39	85.33	7.45	9.69

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Resona Holdings Inc	JP Equity (Nikkei 225)
2	Mitsubishi Motors Corp	JP Equity (Nikkei 225)
3	Mizuho Financial Group Inc	JP Equity (Nikkei 225)
4	Gs Yuasa Corp	JP Equity (Nikkei 225)
5	Japan Airlines Corp	JP Equity (Nikkei 225)
6	Sumitomo Mitsui Financial Group Inc	JP Equity (Nikkei 225)
7	Toshiba Corp	JP Equity (Nikkei 225)
8	Acom Co Ltd	JP Equity (Others)
9	Promise Co Ltd	JP Equity (Others)
10	Sharp Corp	JP Equity (Nikkei 225)

General

There are no specific provisions in Japan dealing with securities lending arrangements, and accordingly, income and expenses related to securities lending transactions are subject to general taxation regulations in Japan. As such, income should be recognized on an accruals basis. In general, expenses should be recorded in the period when, the underlying obligation is fixed, events that directly trigger the payments with respect to the obligation have occurred, and the amount of the expense is reasonably determinable.

Japanese direct tax considerations

For Japanese tax purposes, a lending fee for bonds issued by the Japanese government, municipalities or domestic corporation is treated as Japan source income taxable to a non-resident taxpayer (i.e., business income from assets held in Japan) whether or not the taxpayer has a PE in Japan. This may be exempt by an applicable tax treaty. The tax rate for a foreign company with no PE in Japan would be the national corporate tax rate of 30%. (Domestic companies and foreign companies with a PE are also subject to local taxes, resulting in an effective tax rate of approximately 41%.)

Manufactured payments are generally not treated as dividends. Rather, unless otherwise classified as the lending fees mentioned above, they are treated as payments under contract, and as such, non resident lenders that do not have a permanent establishment in Japan are not subject to any corporate income tax or withholding tax on manufactured payments.

Interest paid to non-residents that do not have a permanent establishment in Japan is subject to withholding tax at 20%. This may be reduced by an applicable tax treaty.

For resident counterparties, the withholding tax treatment would be the same as above, although many financial institutions involved in the stock lending/borrowing business may enjoy an exemption from withholding tax on interest. The key difference for resident companies would be that they would have to include any income and expenses earned through the stock lending/borrowing business in calculating their taxable income.

For Japanese tax purpose, the lender would not treat the securities loan as a sale, but rather a financing transaction, debiting the collateral received to Cash and crediting a payable to the borrower. Accordingly, no capital gains tax implications should arise.

Other taxes and considerations

Lending fees should not be subject to Consumption Tax.

Documentation signed in Japan in respect of securities lending arrangements should generally be subject to stamp taxes, at a minimal rate (JPY 200).

Based on information current as at 1 January 2010

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Graph 1 - Japan Equity

Graph 2- Security of the Year
Japan Airlines Corporation

Graph 3 - Japan Airlines Corporation

All graphs and tables have been sourced using the Data Explorers suite of products.

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A Taxing Year for the Lending Industry

Taxation considerations have always loomed large in the securities lending industry. Indeed, the efficacy of securities lending transactions is often dependent on the right tax outcome. In 2009, there were a number of significant tax developments that are likely to shape the industry in years to come. We have set out below some of these developments as there are likely to continue to be important in 2010.

US Senate Hearing

The hearing entitled "Dividend Tax Abuse: How Offshore Entities Dodge Taxes on U.S. Stock Dividends" primarily focused on equity swap transactions that allegedly enabled investors to sidestep US dividend withholding taxes. During its investigation, the Subcommittee found that phrases like "dividend enhancement," "yield enhancement," and "dividend uplift" were being used to describe products which it regarded as abusive. It was also found that Notice 97-66 regulating foreign-to-foreign lending, despite it sourcing and characterisation rules, was proving ineffectual in preventing abusive transactions.

These developments have culminated in the tabling of proposed legislation referred to as FATCA (Foreign Account Tax Compliance Act of 2009), that seeks to revoke Notice 97-66 and introduce a more wide-ranging concept of a 'dividend equivalent' which includes the dividend income element embedded within derivative contracts as well as substitute (manufactured) payments arising under lending arrangements.

Global Master Securities Lending Agreement ('GMSLA') 2009

In July 2009, International Securities Lending Association (ISLA) published the 2009 version of GMSLA. The GMSLA 2009 updates the previous industry standard master agreement GMSLA 2000, with a number of important and significant tax enhancements. The tax related changes included:

In general, greater clarity around tax terms and certain tax matters;

manufactured dividends on lent securities to be agreed between the parties or otherwise to be equivalent to the gross amount paid by the issuer, assuming no withholding or deduction for tax;

manufactured payments arising on non-cash collateral paid by the lender to the borrower to be equivalent to the amount that would have been received by the lender after any applicable withholding or deduction for tax;

an updated UK tax addendum.

Notwithstanding the positive changes, the new GMSLA is unable to cover all relevant tax issues. It was never the intention for the document to provide for all possible tax matters. Indeed, whilst there is a UK tax addendum addressing UK tax issues, the agreement is silent in the case of other important jurisdictions such as the US.

Beneficial Ownership

The concept of beneficial ownership has been important in international tax law, and particularly so within the securities finance industry. The last 12 months has seen changes in the approach of tax authorities in their application of the concept of beneficial ownership.

For example, in Italy, new legislation introduced in April 2009 provided that dividends received by the borrower under securities lending arrangements would be essentially subject to the relevant tax implications applicable to the original lender, as if the securities had not been lent. However, such provisions have not been subject to any official explanation by the Italian tax authorities (as at the end of 2009) and therefore the practical application of the new regime and the documentation requirements to be met in order to transfer to the borrower the tax position of the lender are not entirely clear. In this regard, we are aware that participants in the Italian market (e.g. financial intermediaries acting as lending agents) are monitoring these types of transactions and exploring alternative solutions that may take the transactions out of the scope of the new provisions.

Another example would be the Swiss tax authorities, who have launched a general investigation in 2009 in connection with perceived dividend stripping transactions. The investigation saw numerous financial institutions (including UK banks) receiving information request letters from the authorities questioning the economic rationale of the transactions and also requesting details of the relevant counterparties involved (including residence). Specifically, Danish banks and financial institutions were first to be investigated since the Swiss-Denmark tax treaty allowed for a full withholding tax refund.

Similar information request letters were also seen from the Finnish tax administration, asking foreign investors detailed questions about their rights and entitlements under Finnish securities. We understand that a particular focus is placed on dividends flowing from Finland to UK, which is not surprising given London's role as the principal financial centre for the Nordic markets and the zero withholding tax for portfolio investors under the Finland-UK tax treaty.

The changing attitude of tax authorities and the recent actions taken together can be seen as, at least in part, a product of the recent International Fiscal Association round table and international discussion of the concept of beneficial ownership. Certainly, these global developments have also led to an increased awareness by the industry of the relevant tax issues surrounding securities lending transactions, particularly in a cross border context.

EU Discrimination Cases

A number of European Court of Justice cases have emerged in recent years which successfully challenged the withholding rules applied to dividend payments arising from various members states. The most recent case, the Aberdeen decision, is in line with the Denkavit and Amurta decisions which dealt with tax discrimination in regards to withholding taxes on outbound dividends. These cases have provided the basis for the reclaim of withholding taxes by investors on the grounds that rules applied by some member states result in a different treatment between domestic and overseas recipients of dividends.

The issue of whether and how the case law should apply for entities making claims to recover withholding taxes on manufactured payments on certain stocks (rather than actual dividends) raises fundamental questions around the impact on securities lending agreements, including the pricing of contracts. We would expect some of these issues to be further explored in 2010.

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OECD Treaty Benefits and Collective Investment Vehicle

In December 2009, the OECD released its Report on the Granting of Treaty Benefits with respect to the Income of Collective Investment Vehicles. This update of the earlier January 2009 report, proposes changes to the commentary to the OECD model treaty dealing with the question of the extent to which collective investment schemes or their investors are entities to treaty benefits. One suggestion in the report is to apply an effectively transparent approach for the purposes of securing treaty benefits.

Whilst the report considers in detail the relevant technical issues, the practical issues of how a transparent approach would apply, particularly in securities lending arrangements, would need to be addressed. The report remains in draft form and consultation on the draft continues into 2010.

Conclusion

Overall, given the taxation developments impacting the industry, the major theme of tax derisking is likely to dominate 2010.

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Europe

European Government Bonds

If 2008 was characterized by the peak of the banking crisis, 2009 can best be described as being a year of steady recovery.

Financial markets relied more heavily than usual on Governments and central banks to pilot them out of the financial crisis. The year can be split into two cycles:

- 1st period from January to May 2009: common policy to lower interest rates and supply liquidity
- 2nd period from June to December 2009: oversupply of cash

General interest rate cut: January to May 2009

Major central banks cut their interest rates, reaching historic lows.

European money markets, with the support of the ECB, started to normalise, with the best rated issuers' spreads at 50bp. One month before, they were at 150bp.

During the 1st quarter of 2009 the volume of European Government bond issues greatly increased as Governments strived to boost their economy. The influx of paper weighed heavily on the Stock Loan or Repo activity with fees being slashed or even negative for some of the lowest rated, non-core Government bonds. German and French bonds fell to between 1 to 2bp while Italian and Spanish Government bonds were lent at – 2 to - 5bp. The need to maintain cash balances for reinvestment programs may explain these levels.

During the first 5 months of 2009 the main central banks used a full range of tools to avoid the financial system coming to a standstill.
In addition to liquidity facilities:

- BOE announced that it planned to buy up to GBP 150bn of assets
- FED announced the acquisition of USD 300bn of US Government debt.
- ECB decided to buy EUR 60bn of covered bonds in the primary market.

The Repo market has become essential in financing banking and trading activities and thus performs a role of paramount importance for market liquidity. We have noticed an increasing number of players who favour Repo or non cash collateral transactions over the usual non-collateralised products. Throughout this period, non-cash transactions accounted for two-thirds of all transactions, with the remaining third being cash transactions, which illustrates the decrease in interest for classic money market products.

Oversupply of Cash: June to December 2009

Most significantly, the ECB carried out its first LTRO 12 months for EUR 443bn. This long term influx of liquidity had several positive effects:

- normalisation of the money market; 10bp on a 3 month bank issue.
- low EONIA, 65bp below the official ECB rate.
- Repo transactions were used as an investment product, generating margins of 8 to 9bp for French and German debts (more interesting than the BTF or BUBILL

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
European Government Bonds	1,039,555.30	395,542.10	32.19	8.73	3.04	6.40
France Bonds (Govt)	209,024.60	94,167.00	31.77	8.18	2.95	6.60
UK Bonds (Govt)	227,170.10	111,086.60	46.62	10.04	4.75	6.65
Italy Bonds (Govt)	104,522.90	19,546.20	20.23	0.73	-0.23	2.25
Switzerland Bonds (Govt)	33,616.40	9,260.40	32.83	24.03	8.20	8.21
Netherlands Bonds (Govt)	71,426.30	27,135.80	33.44	7.27	3.14	7.75
Germany Bonds (Govt)	215,886.70	98,818.60	33.41	9.32	3.30	9.29
Portugal Bonds (Govt)	10,060.30	1,329.50	11.59	5.36	0.63	2.22
Spain Bonds (Govt)	39,112.30	6,451.10	20.78	9.14	1.87	4.81
Sweden Bonds (Govt)	10,569.50	1,169.10	8.77	13.79	1.26	2.28
Finland Bonds (Govt)	9,022.70	2,850.20	23.88	3.39	0.76	7.32
Denmark Bonds (Govt)	5,916.40	1,052.40	11.20	8.09	0.95	4.00
Austria Bonds (Govt)	27,512.00	7,861.00	25.88	13.37	3.62	5.99
Belgium Bonds (Govt)	30,286.80	8,912.50	22.49	8.05	2.15	4.23
Greece Bonds (Govt)	18,762.10	2,863.70	15.63	-3.40	-0.69	0.55

over equivalent periods, 5 to 6bp for the rest of the European debt).
- with fewer borrowers, quarter-end pressure in Europe was less significant than the level observed in previous years.
- The main consequences of the covered bonds' purchase programme were the tightening of the spread on the cash market, and the decrease from 12 – 15bp to 4 – 6bp on the GC Repo market.

The Greek crisis and rumours of new rules on covered bonds' ratings has reinforced a situation whereby spreads vary enormously between core and non-core European Government bonds. This hierarchy is also noticeable between high-rated supra and jumbo issues. Italian Government bonds had previously been quoted at up to 10bp over German bonds, with jumbo issues 5bp higher still. Greek bonds became very illiquid at this time. While this oversupply of cash could have brought the levels for reverse repos down, the increased interest in short term repos helped maintain interesting returns.

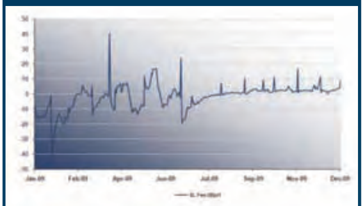
The Euro zone experienced the widening of bond market spreads, which, although negative for lenders, was profitable overall, via reverse repos, for a reinvestment approach.

Table 2 - Security Rankings by Total Daily Return

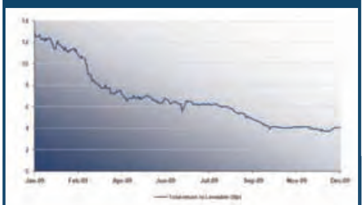
Rank	Stock Description	Security Type
1	France (Government) (5.75% 25-Oct-2032)	FR Dom Govt Bond (Fixed Rate)
2	Bundesrepublik Deutschland (3.75% 04-Jan-2015)	DE Dom Govt Bond (Fixed Rate)
3	France (Government) (4% 25-Apr-2013)	FR Dom Govt Bond (Fixed Rate)
4	France (Government) (4% 25-Apr-2013)	FR Dom Govt Bond (Fixed Rate)
5	Bundesrepublik Deutschland (4.5% 04-Jan-2013)	DE Dom Govt Bond (Fixed Rate)
6	Germany (4.25% 12-Oct-2012)	DE Intl Govt Bond (Fixed Rate)
7	Bundesrepublik Deutschland (5.625% 04-Jan-2028)	DE Dom Govt Bond (Fixed Rate)
8	France (Government) (3.5% 25-Apr-2015)	FR Dom Govt Bond (Fixed Rate)
9	United Kingdom Of Great Britain And Northern Ireland (Government) (2.5% 16-Apr-2020)	UK I/L Dom Govt Bond (Fixed Rate)
10	Bundesrepublik Deutschland (4% 04-Jan-2037)	DE Dom Govt Bond (Fixed Rate)

Graph 1 - European Government Bonds

Graph 2 - European Government Bonds



Graph 3 - European Government Bonds



All graphs and tables have been sourced using the Data Explorers suite of products.

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France

Holders of large cap French equities had a good year in 2009 demonstrating why French portfolios are one of the favourites for lenders and borrowers alike. French government earnings drifted back to 2007 levels.

Market Analysis

French equities are always a strong earner for lenders and earnings were substantially higher in 2009 with TRTL increasing from 36.53bp to 42.37bp – the driver for the uptick was increased securities lending fees across all equity indices as utilisation stayed relatively steady. Yield enhancement opportunities were strong with a longer impact in 2009 lasting from mid April to early June rather than the shorter spike of returns seen in 2008.

One early warning sign for the coming year is the lower utilisation of securities at year-end which could potentially see lower revenues in the first quarter of 2010.

The French Regulator, AMF, has continued its short selling restrictions through 2009 and they will be retained until the end of January 2010 when it will consider its next steps.

French government bonds reversed the securities lending earnings gain seen in 2008 as fees dropped back. Utilisation remained consistently around the 30% mark but TRTL fell back to 6.6bp from 10.74bp a year earlier.

Significant Securities

Not much change in the top 10 earners but actually that is what makes the French equity portfolio so attractive. The big dividend payers continue to top the lending charts and we would be surprised if this changes in 2010.

One significant change from 2008 was the additional interest shown in some securities that were involved in capital raising activities in late 2009 – Axa, BNP Paribas and Societe Generale all announced significant rights issues in October and November that saw utilisation spike for a short period of time.

Lafarge hit the top 10 for the first time following announcements in late 2008 that it was seeking to sell assets and subsequent capital raising efforts – this saw utilisation increase from 30% to 70% in November 2008, a situation that did not return to normal until May 2009.

Carrefour saw its utilisation also increase from a typical level of 20% to a peak of 60% in May 2009. The climb was a slow one that actually stretched back to July 2008 but utilisation didn't return to normal until July 2009 providing good returns for those who were lending Carrefour shares.

Security of the Year

GDF Suez SA, our Security of the Year for the last 2 years, will breathe a sigh of relief – it has been superseded this year by Lafarge. Extracting itself from some debt problems led to a combination of asset sales and capital raising that is all of interest to borrowers. Although relatively low in the top 10 the story was more interesting than other pure yield enhancement plays. Reassuringly for Lafarge the company's utilisation has now returned to 20% and its share price has doubled since March 2009.

Outlook

We called for excitement last year in France but, in hindsight, a little tranquillity is a good thing – particularly in recent markets. France will always be an important market for securities lending and we suspect good returns will be made again in 2010.

The market will also be keeping a close eye on the AMF's next steps on short selling regulation. Given the AMFs influence in consultations on short selling globally this will be important to monitor.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
France Equity	229,493.00	57,843.30	24.16	123.65	38.97	42.37
France Equity (CAC40)	196,944.40	51,430.60	24.74	121.23	40.33	43.73
France Equity (others)	6,306.90	534.90	13.01	164.66	19.93	21.33
France Equity (SBF80)	26,241.70	5,877.80	22.38	129.57	33.38	37.32
France Government Bonds	209,024.60	94,167.00	31.77	8.18	2.95	6.60
France Govt Bonds (Domestic)	192,941.50	91,766.00	33.02	8.10	3.02	6.71
France Govt Bonds (International)	16,083.10	2,401.00	14.84	11.86	2.01	5.06

Table 2– Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Total Sa	FR Equity (CAC)
2	France Telecom Sa	FR Equity (CAC)
3	Sanofi-Aventis Sa	FR Equity (CAC)
4	Gdf Suez Sa	FR Equity (CAC)
5	Vivendi Sa	FR Equity (CAC)
6	Bnp Paribas Sa	FR Equity (CAC)
7	Lafarge Sa	FR Equity (CAC)
8	Axa Sa	FR Equity (CAC)
9	Carrefour Sa	FR Equity (CAC)
10	Societe Generale	FR Equity (CAC)

General

Securities lending arrangements in France are normally structured as two sales and are, accordingly fully taxable transactions.
However, there are two main types of securities lending transactions which benefit from a favorable French corporate income tax regime (no taxation of capital gains):

- "prêt de titres", i.e. a securities lending agreement;
- "pension livrée", equivalent to a "repo" contract.

French direct tax considerations

The following conditions need to be met to benefit from the capital gains neutral tax regime on these transactions:

- securities cannot be subject to "pension livrée" or "prêt de titres" if, during the lending period, a dividend giving rise to a foreign tax credit is distributed, or interest subject to withholding tax or giving rise to a foreign tax credit is paid;
- the securities must actually be returned at the end of the lending period. In this respect, this condition will be met, even if the securities returned to the lender are not the same as the securities originally lent, provided that they are fungible with the original securities.

The remuneration paid by the borrower to the lender would be tax deductible for the borrower (under the general deductibility conditions and in particular provided it complies with the arm's length principle) and fully taxable for the lender (treated as interest) if they are resident in France.
Dividends received by a French resident borrower and paid on to a French resident lender should not benefit from the French parent/subsidiary regime and accordingly, should be taxable at the standard CIT rate (effective rate of 34.43% in 2010). This should apply whether the lending transactions benefit from one of the tax favorable specific lending regimes described above, or not. A tax deduction should be available for the manufactured dividend provided it meets the general tax deductibility criteria.

Where there is a non-resident lender and a resident borrower, the manufactured dividend paid by the borrower to the lender would be within the scope of French withholding tax. However, from a French legal and tax perspective, it is uncertain as to whether the manufactured dividend will be deemed to be (a) consideration for services (domestic withholding tax equal to 1/3 of the gross amount paid, subject to applicable tax treaties), (b) interest (unlikely, no domestic withholding tax as from March 1, 2010, if not paid to an entity located in a tax haven) or (c) an additional part of the purchase price paid by the borrower for the securities (not subject to French withholding tax except if the lender owns more than 25% of the shares). This would primarily depend on the documentation entered into for the lending transaction.

Other taxes and considerations

Finally, transfer tax on the sale of securities should apply to securities lending arrangements (at the rate of 3% or 5%, with potential capping to 5,000 € per transaction depending on the nature of the security), except for "pensions livrées" that benefit from a specific exemption.

Based on information current as at 1 January 2010

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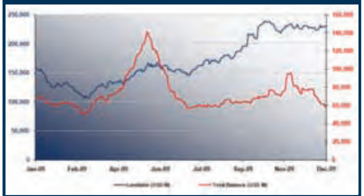
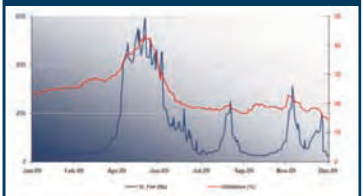
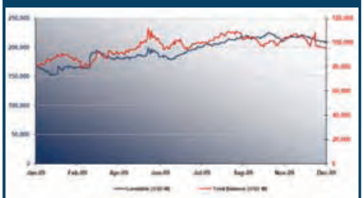
Graph 1 - France Equity



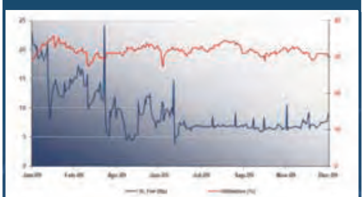
Graph 2 - France Equity



Graph 3 - France Government Bond



Graph 4 - France Government Bond



Graph 5 - Security of the Year
Lafarge S.A.

All graphs and tables have been sourced using the Data Explorers suite of products.

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Germany

Lenders of German equities saw increased revenues in 2009 as a result of increased fees but government bond holders saw returns fall back in the second half of the year.

Market Analysis

Lenders of German equities benefited from the global trend towards intrinsic lending – receiving higher fees for the stocks most in demand. This is especially true of lending over dividend dates. As a result, the average TRTL increased by around 50% to 26.50bp driven by average SL fees increasing from 72.46bp to 121bp. Utilisation did fall back slightly from over 20% to 18% but making more money from less transactions has to be good news for lenders. The fall in utilisation was particularly noticeable at the end of the dividend season with average utilisation dropping from 28% to 15%.

German government bonds continued to be in demand with utilisation increasing during 2009 from 30% to 35%. However, the average utilisation of 33.41% is well below that seen in 2008 leading to TRTL for this asset class to fall back from 13.33bp to 9.29bp. Some of this reduction in return is due to reinvestment returns also falling back from the peaks of 2008 as money market yields reduced and lenders moved to shorter term, lower yielding securities.

German regulators have applied a relatively light touch regulation to short selling thus far with a ban on naked short selling.

Significant Securities

Germany had the global security of the year in 2008 – the Volkswagen/Porsche saga was as we noted last year, one of the most extraordinary events ever observed.

Outside of that bubble of excitement though, things are pretty consistent. As we noted above, most of the value in German securities comes from lending over dividend dates therefore most returns are achieved during the first few months of the year. All the big names on our top 10 earners are in the table due to this activity when utilisation increases from 40% to 70% before falling back to normal utilisation levels of around 10 – 15%.

Volkswagen shows up again in this year's top 10 primarily as a result of the sudden jump in utilisation in August that saw it rise from 18% to 80%. The share price fell from EUR250 to EUR75 at year end.

Security of the Year

A new name in the Top 10 this year is Q Cells – a solar cell specialist. Announcements of a link up with China's LDK Solar sparked interest especially when the relationship came under pressure later in the year. However, the real driver of interest in borrowing Q Cells was led by their issuance of convertible bonds. Securities lending fees during the later part of the year reached 15%.

Outlook

Despite the specific interest in Q Cells and Volkswagen, it is dividend related trading that will drive revenues once again in 2010. Early signs are that returns are likely to be higher than those seen in 2009 with demand and fees, pushing slightly higher – good news for many lenders who make significant securities lending revenues from their German equity portfolios.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Germany Equity	188,624.80	38,610.70	18.39	121.00	24.40	26.50
DE Equity (DAX)	157,038.00	32,800.30	19.35	110.57	25.02	27.18
DE Equity (MDAX)	15,517.30	2,699.90	16.54	136.00	23.71	25.94
DE Equity (SDAX)	1,212.20	193.30	13.79	138.47	21.29	22.52
DE Equity (Others)	14,857.40	2,917.20	12.39	213.03	22.89	24.51
Germany Government Bonds	215,886.70	98,818.60	33.41	9.32	3.30	9.29
Germany Govt Bonds (Domestic)	175,262.60	89,137.50	36.34	9.38	3.63	9.72
Germany Govt Bonds (International)	40,624.20	9,681.00	8.95	20.68	1.88	7.42

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	E.On Ag	DE Equity (DAX)
2	Basf Se	DE Equity (DAX)
3	Allianz Se	DE Equity (DAX)
4	Bayer Ag	DE Equity (DAX)
5	Rwe Ag	DE Equity (DAX)
6	Muenchener Rueckversicherungs Gesellschaft Ag	DE Equity (DAX)
7	Siemens Ag	DE Equity (DAX)
8	Volkswagen Ag	DE Equity (DAX)
9	Q Cells Se	DE Equity (Others)
10	Daimler Ag	DE Equity (DAX)

General

German GAAP and tax accounting rules do not provide for specific accounting rules for securities lending arrangement (Wertpapierleihe). Under the applicable general accounting rules the loaned securities are transferred from the lender's balance sheet to the borrower's balance sheet as not only the legal ownership but – according to the prevailing interpretation - also the economic ownership of the securities is transferred to the borrower during the lending period. However, given the nature of the security lending arrangement as a loan in kind (Sachdarlehen) the transfer of the securities doesn't lead to a realization of any hidden profits as a corresponding claim to re-transfer the securities to the lender is accounted for in the balance sheets.

German direct tax considerations

Non-German resident lenders/borrowers are only subject to German non-resident taxation with certain income deriving from German sources. Any lending fees and the manufactured dividends are not subject to German non-resident taxation and therefore basically also not subject to German withholding tax.

Interest income on any cash collateral received by a non-German resident lender is not subject to German non-resident taxation unless the loan is collateralized with German real estate and the right to tax such interest is not attributed to the state of residence under an applicable double tax treaty.

For German resident lenders/borrowers:

Any dividends received by a resident borrower during the loan term of loaned equities are subject to the German participation exemption rules, i.e. the dividends are effectively 95% tax exempt as 5% of the gross dividends received are treated as non-deductible business expenses. The participation exemption rules do not apply to banks and financial institutions holding the equities as current assets as well as to life and health insurance companies. The resident borrower is entitled to deduct German dividend withholding tax on the dividends received from the loan securities from its own tax liability.

Any lending fees as well as the manufactured payments received by the lender are fully taxable (the German participation exemption rules do not apply to manufactured dividends). Lending fees as well as manufactured payments are tax deductible for the borrower for German tax purposes. However, effective as of 2007 an anti-avoidance regulation has been introduced under which a deduction is not available where (1) the equities are lent from the current assets of a German resident bank or financial institution as well as from a German life and health insurance company, (2) the borrower is entitled to the benefits of the German dividend participation exemption and (3) the equities are lent over the dividend payment date.

Lending fees and the manufactured dividends remain tax deductible as long as the manufactured dividend has been subject to a withholding tax. Basically, no dividend withholding tax applies on manufactured dividends. However, a 15% withholding tax applies to lending fees and manufactured dividends paid to certain German public bodies and tax exempt corporations.

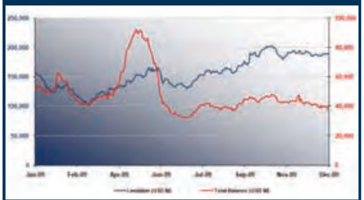
Interest income on any cash collateral received by the lender is fully taxable in Germany.

Other taxes and considerations

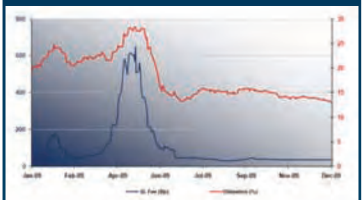
Germany does not levy any indirect (VAT) or transfer taxes on securities lending transactions.

Based on information current as at 1 January 2010

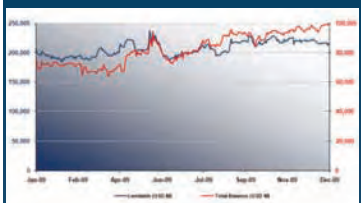
Graph 1 - Germany Equity



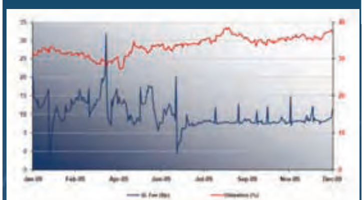
Graph 2 - Germany Equity



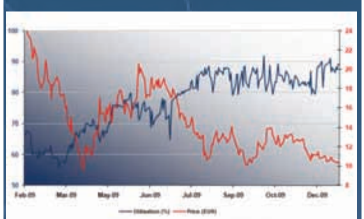
Graph 3 - Germany Government Bond



Graph 4 - Germany Government Bond



Graph 5 -Security of the Year
Q Cells SE



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Italy

The Italian short selling regulations provided a few operational issues for practitioners in 2009 and future developments will be watched with interest. Revenue wise, large cap Italian equities continue to be a core component of a securities lending portfolio, particularly for non-EEA institutional investors, although revenues are flat year-on-year.

Market Analysis

Italian equities are another asset class to have seen falling utilisations that have been compensated for by increased SL fees. Average utilisation has fallen 3% but average fees have increased by 30% resulting in TRTL that are in line with 2008. It is worth noting that at the height of dividend related activity 2009 fees were more than twice those of 2008 but this is reflective of shorter duration trades on all three occasions.

Lendable balances have increased during 2009 in line with market performance but loan balances, dividend period activity excepted, have been flat. While SLRTL tables are broadly in line with 2008 in each index, the MIDEX halved utilisation in 2009 and experienced a similar reduction in investment yield pick up as expressed by comparing TRTL to SLTRL. This is more exaggerated than in the MIB30 and other indices and may reflect a concentration of supply in the hands of few lenders that either switched collateral to non-cash or reigned in their cash reinvestment activity.

Significant Securities

The usual suspects make an appearance in the top 10 securities in 2009 in the form of Eni Spa, Enel Spa, Telecom Italia Spa and Assicurazioni. However here the trend ends. New entrants include Mediaset Spa, the communications and broadcasting group, Atlantia Spa, the holding company of the construction giant Autostrade per l'italia, that saw a doubling of its share price in 2009 and Snam Rete Gas Spa the gas supplier that provided SL fees in excess of 10 % and 4% respectively in 2009. Absent from the top 10 are Intesa Sanpaolo, Unicredit and Banca Monte Di Paschi but this is hardly surprising given the short selling policy on bank stock during its seven month duration.

Security of the Year

No obvious choice in 2009 as dividend related transactions took precedence over directional plays. The top 10 securities in terms of average daily return largely mimicked typical utilisation for biannual dividend related stocks albeit with higher fees and shorter duration. The exception to the group is Bulgari Spa, a leading global player in the luxury market that saw its share price rise from around EUR 2.76 in March to a high of EUR 6.46 in November. Presence in new markets such as China certainly may have aided this gain. Its post dividend season activity saw utilisation above 50% for the majority of the remainder of the year with fees hovering above 300bp. The July rights issue generated a lot of short interest which lasted throughout the remainder of the year. Tiscali Spa was in very short supply during its rights issue which drove SL fees to astronomical heights albeit on the thinnest of volume. For those that held the stock however, an average fee of 450% was not to be sniffed at.

Outlook

Italy has been a hugely significant market over the years but not without its moments of controversy with the morass of tax considerations and regulatory challenges. In all, 2009 weathered a difficult year well. Approved reduced withholding tax rates applicable to EU/EEA resident pension funds to 11% will affect the value of dividend related activity in 2010 but clarification as to eligibility and required documentation will need to be established.

Reduced withholding for European corporate tax paying entities to 1.375% takes more value out of the Italian lending market and 2010 will likely be see those institutions with deeper withholding tax rates benefit more than ever in a less crowed market during the dividend season.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Italy Equity	62,511.40	10,819.50	13.47	147.79	31.24	33.45
Italy Equity (MIB30)	54,478.40	8,918.20	13.51	140.82	31.26	33.47
Italy Equity (MIDEX)	2,556.30	383.30	11.78	162.86	23.21	25.28
Italy Equity (Others)	5,476.70	1,517.90	13.88	175.81	34.18	36.40
Italy Government Bonds	104,522.90	19,546.20	20.23	-0.73	-0.23	2.25
Italy Govt Bonds (Domestic)	99,919.90	18,525.50	20.19	-1.30	-0.37	2.08
Italy Govt Bonds (International)	4,603.00	1,020.70	21.10	11.22	2.51	5.71

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Eni Spa	IT Equity (MIB30)
2	Enel Spa	IT Equity (MIB30)
3	Mediaset Spa	IT Equity (MIB30)
4	Telecom Italia Spa	IT Equity (MIB30)
5	Assicurazioni Generali Spa	IT Equity (MIB30)
6	Telecom Italia Non-Conv Svgs	IT Equity (Others)
7	Atlantia Spa	IT Equity (MIB30)
8	Snam Rete Gas Spa	IT Equity (MIB30)
9	Terna - Rete Elettrica Nazionale Spa	IT Equity (MIB30)
10	Bulgari Spa	IT Equity (Others)

General

There are no specific rules for securities lending arrangements in Italy and the parties are free to agree terms and conditions of the relevant arrangement.

Italian direct tax considerations

In principle, proceeds (i.e. lending fees) deriving from securities lending which have been realized by non-resident entities are subject to withholding tax at the rate of 12.5% (or the reduced rate provided for by the applicable tax treaty, if any) except for manufactured dividends which are subject to withholding tax at the rate of 27% (or the reduced rate provided for by the applicable tax treaty). Note that since April 2009, new Italian legislation applies such that dividends received by the borrower under securities lending arrangements would be essentially subject to the relevant tax implications applicable to the lender, as if the securities had not been lent. Accordingly consideration to these rules should be given in the case of cascading trades.

Non-resident entities may benefit from a domestic withholding tax exemption which may apply to proceeds from securities lending except for manufactured dividends. The exemption applies to entities resident in Countries allowing an adequate exchange of information with the Italian tax authorities to the extent that a proper documental procedure has been implemented. Certain anti-abuse provisions are in place for non-resident entities.

Should the Borrower be a resident company, proceeds from securities lending would be included within the overall taxable income (without being subject to withholding tax) subject to corporate income tax at the rate of 27.5%. Proceeds realized by banks, financial institutions and insurance companies would also be subject to local income tax at the rate of 3.9 % up to 4.82%.

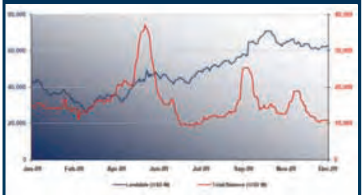
Other taxes and considerations

Securities lending arrangements are exempt from VAT. Registration tax is due on the relevant agreement at the flat rate of Euro 168.00 in case of use. There is no transfer taxes/stamp duty on securities lending transactions.

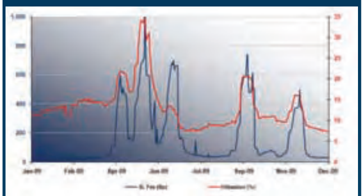
Based on information current as at 1 January 2010

Deloitte.

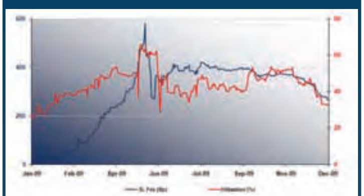
Graph 1 - Italy Equity



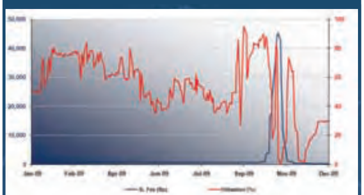
Graph 2 - Italy Equity



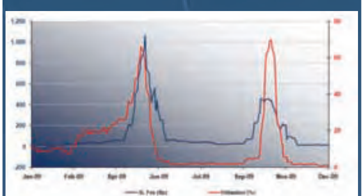
Graph 3 - Bulgari SpA



Graph 4 - Tiscali SpA



Graph 5 - Snam Rete Gas SpA



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Netherlands

2009 was a slightly bland year for lenders of Dutch securities which probably represents good news for the Dutch companies after the travails of 2008! With the upturn in M&A activity expected in 2010 the next 12 months looks more promising.

Market Analysis

The Dutch market has seen recovery in terms of the quantity of lendable assets. Though the figure has not returned to the highs recorded in 2007, there has been a 37% increase in lendable assets over the past year. The annual trend of lendable assets closely mirrors the performance of the AEX Index in 2009, which also saw gains of 37% over the year. Also, growing confidence in the markets could have led to the introduction of new lenders and the return of others to lending programmes. A short term surge in lendable assets was observed in Q2 2009. During this time the ban on short selling was also lifted in the Netherlands. In comparison with other leading European markets, the Netherlands is paving the way to recovery in parallel with Germany.

Despite rising balances, the securities lending return to lendable (SLRTL) of equities saw little movement as it decreased marginally by 0.48bp. This follows from utilisation seeing minimal change and the SL fee falling just 1bp since 2008. However government bonds reach a similar conclusion through a different story. Government bonds saw the SL fee increase by 24.23bp. This was counteracted by a significant fall of 45.8% in utilisation resulting in the SLRTL also falling by 1.4bp. The results see both equities and government bonds with similar bp for TRTL, in contrast to 2008 when government bonds saw a significantly higher TRTL.

The Dutch regulator, AFM, finally lifted the ban on short selling of financial securities at the end of May but still requires disclosure of short obligations. The ban which came in to play in September 2008 was extended several times.

Significant Securities

The top 10 securities ranked by total daily return have seen a reshuffle of ranking with some new entries for 2009. Names which continue to make the list this year following last year are seen to have moved up the rankings with the exception of Reed Elsevier Nv which has dropped to eighth place. Topping the list we see commodities industry giants, Arcelormittal Sa and Royal Dutch Shell Plc.

Many of the big names are in the Top 10 based on increases in interest around dividend dates so we look to the bottom of the chart for some more interesting stories.

TomTom NV is a far cry from its days of share prices of EUR 65 on the AEX Amsterdam index in 2007. Though TomTom outperformed the index in 2009, its relative performance over the year was mixed. A rights issue over the summer months to repay debt saw the security behave typically of one executing a rights issue. On completion, utilisation fell from 90% to 20% and short base fell from 12% to 2%. Leading providers of portable navigation devices TomTom and US company Garmin were hit by Google's announcement of an upgrade to its smart-phone software to include a free navigation feature. TomTom has since seen its short base increase to 12% with lendable quantity falling from 20 mn to 13 mn. Utilisation has increased back to its earlier high of 90%. 2010 will see TomTom go ahead with plans to penetrate the North American, Mexican and Argentinean markets.

Heineken Nv enters the bottom of the ranking this year as its performance improved over the course of 2009. This follows a mixed year marked with acquisitions in line with a bold plan to conquer the stalling Western European beer markets during turbulent times. Similar to ArcelorMittal Sa, this security also sees much of its revenue activity as a result of dividend trading. Over the year utilisation has decreased from 15% to 4%. Similarly, the short base fell in the second half of the year from an average of 3% to 1% shares outstanding as profits were reported and investor confidence grew. Lendable quantity rose significantly at the end of the first quarter from 55 mn to a high of over 70 mn by the end of the year.

Security of the Year

ArcelorMittal Sa has moved up five places since 2008 to become ranked the top security by total group return in 2009. Like the majority of Dutch securities, revenues for ArcelorMittal are the result of several dividend transactions over the year. This dividend activity saw utilisation spike from an average of 20% to over 40% on each of the four dividend dates. Dividends aside, ArcelorMittal has seen an upwards trend in its short base (percentage shares outstanding on loan) over the year – a trend we noticed in last year's Yearbook. In comparison to 2008, when the short base averaged 2%, in 2009 this figure jumped to 7% confirming a growing interest in borrowing of ArcelorMittal shares. However, the lendable quantity also saw a rising trend in 2009 from 120 mn to 200 mn, averaging 165 mn, in comparison to an average of 55 mn in lendable quantity in 2008, which remained constant over the year.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Netherlands Equity	85,675.00	12,915.50	14.41	44.98	6.12	7.45
Netherlands Equity (AEX)	79,370.90	12,183.10	14.60	43.63	5.99	7.34
Netherlands Equity (AMX)	4,370.40	595.30	13.88	75.50	10.22	11.84
Netherlands Equity (Others)	1,933.70	137.10	62.81	9.58	4.84	5.25
Netherlands Government Bonds	71,426.30	27,135.80	7.27	33.44	3.14	7.75
Netherlands Govt Bonds (Domestic)	62,229.20	25,971.50	36.00	7.12	3.35	8.24
Netherlands Govt Bonds (International)	9,197.10	1,164.20	14.06	10.74	1.55	3.99

Outlook

2010 should be a better year than 2009 for a variety of reasons not least the increase in M&A activity and, hopefully, a stronger dividend story. 2009 was a year of consolidation, a common story, but 2010 could be the year when the Dutch market becomes more interesting once again.

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Arcelormittal Sa	NL Equity (AEX)
2	Royal Dutch Shell Plc	NL Equity (AEX)
3	Unilever Nv	NL Equity (AEX)
4	Koninklijke Kpn Nv	NL Equity (AEX)
5	Koninklijke Philips Electronics Nv	NL Equity (AEX)
6	Akzo Nobel Nv	NL Equity (AEX)
7	Asml Holding Nv	NL Equity (AEX)
8	Reed Elsevier Nv	NL Equity (AEX)
9	Tomtom Nv	NL Equity (AEX)
10	Heineken Nv	NL Equity (AEX)

General

In the Netherlands, no specific tax rules apply with regard to securities lending arrangements.

Dutch direct tax considerations

For portfolio investments (i.e. holding less than 5% of the shares), a non Dutch entity/individual receiving Dutch dividends will be subject to Dutch dividend withholding tax. The Dutch domestic rate is 15% which may be lowered as a result Dutch domestic law or based on applicable tax treaties.

The borrower (as the legal owner of the securities) is usually considered as the beneficial owner of the shares and the dividends received (unless the borrower transferred the shares to another party, in which case that party may qualify as the owner). The beneficial owner may be eligible for an exemption, reduction or refund of Dutch dividend withholding tax, provided conditions are met. As the lender in principle keeps the full economical interest in the shares, for corporate income tax purposes the lender does not alienate the shares, although the borrower becomes the legal owner of the shares.

A manufactured payment received by the lender will in principle not qualify as a dividend pursuant to Dutch domestic rules (this may however be different under the US-Netherlands tax treaty). Certain tax exempt entities, such as qualifying EU pension funds, are entitled to a full refund of Dutch dividend withholding tax, provided they qualify as the beneficial owner of the dividends and conditions are met. Anti-dividend stripping rules may preclude the borrower as the beneficial owner, in which case no refund, exemption of reduction of Dutch withholding tax would be available.

For Dutch resident borrowers and lenders, a Dutch entity will be taxable in the Netherlands on its worldwide income (thus both on dividends as well as manufactured payments). Lending fees and interest income on cash collateral are in principle taxable/deductible. As the lender still has the economical interest in the shares, the lender is not treated as disposing of the shares for income tax purposes, although the borrower becomes the legal owner of the shares. With regards to dividend tax, the borrower will in principle qualify as the beneficial owner of the dividends, and may request a refund for Dutch dividend withholding tax and may credit foreign withholding tax on dividends, provided certain conditions are met.

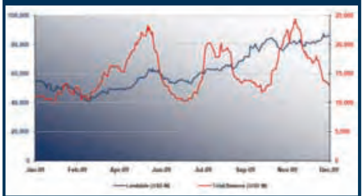
There is no Dutch withholding tax on interest payments.

Other taxes and considerations

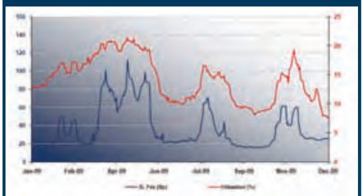
Generally, no Dutch VAT is due on a lending fee and no Dutch transfer taxes are due on securities lending arrangements.

Based on information current as at 1 January 2010.

Graph 1 - Netherlands Equity



Graph 2 - Netherlands Equity



Graph 3 - Netherlands Government Bond

Graph 4 - Netherlands Government Bond

Graph 5 - Security of the Year
ArcelorMittal SA

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Shorts Hiding from the Market in 2009

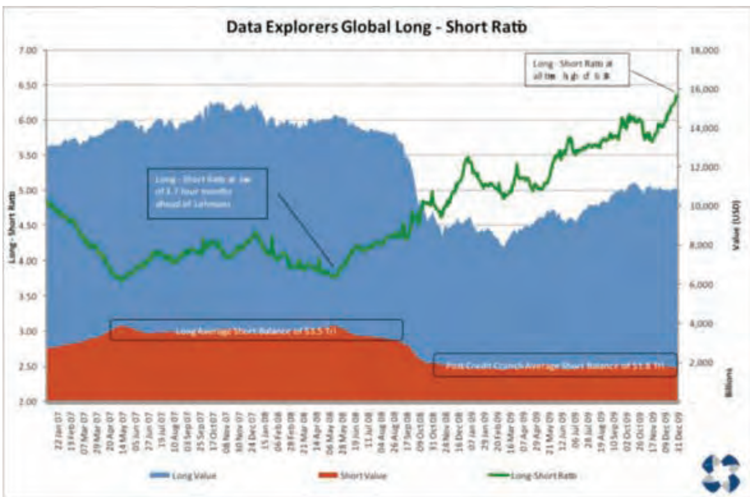
The market turmoil and uncertainty of September 2008 seemed to fade away in March 2009 as markets around the world recovered from their lows. While it was uncertain if the rally would be sustainable, by June it was clear that short sellers were not trying to fight the overall market trend. In fact by the end of 2009, it seemed as if short sellers were playing hide and seek with the market - with them doing far more hiding than seeking for most of the year.

Data Explorers has a number of unique tools to track the volume of securities lending across the global markets. The Data Explorers Securities Lending Indices (DXI), which track the change in loans in relation to shares outstanding for the largest global companies all saw a drop of at least 25% since the start of 2009.

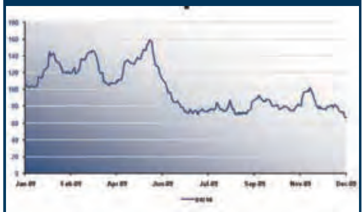
The DXI Global 50 ended the year on its 52 week low , as did the DXI EUxUK 30 and DXI Asiax Japan 30. The DXI UK, while it ended down just over 25% for the year, saw an overall rise in securities on loan since hitting a low in June. This was the only DXI index that saw an overall increase from the summer. The DXI US 30 and DXI Japan 30 saw small increases from the lows they hit in early November.

Another way of tracking sentiment is the Data Explorers Long-Short ratio. This ratio tracks the change in securities lending inventory (longs) vs the amount out on loan (shorts). As you can see from the chart below, the Global Long-Short ratio (which includes both equities and bonds) started rising, mainly due to a decrease in short balance, four months ahead of the Lehman's bankruptcy. Post September 2008 the average global short balance had almost halved from USD 3.5tn to USD 1.8tn. The Global Long – Short ratio closed 2009 at an all time high of 6.34 as inventory levels recovered from the Spring 2009 lows.

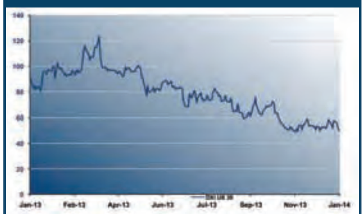
Graph 1



Graph 2 - DXI 50



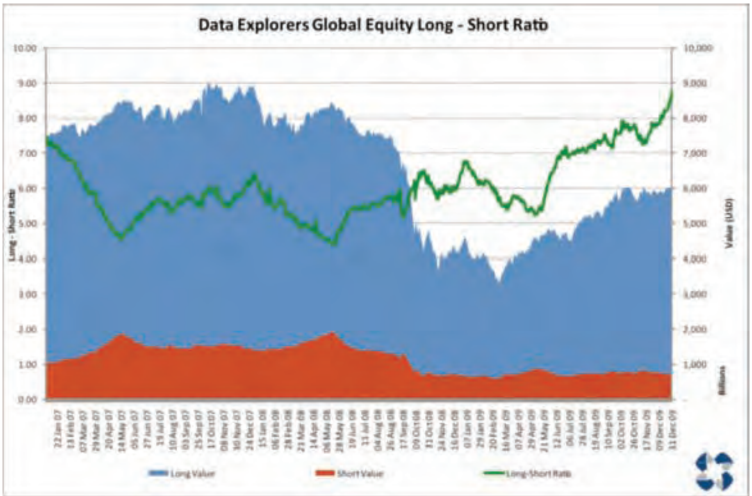
Graph 3 - DXI US 30



Graph 4 - DXI UK 30

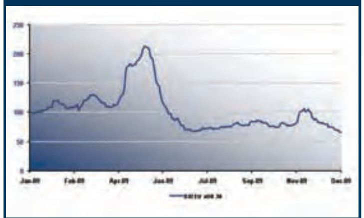
The Global Equity Long – Short ratio also closed the year at an all time high with the ratio up 62% from the low in May 2009. The increase in the ratio was, again, more due to an increase in the amount of inventory available to borrow. At the end of the year the ratio was just under nine – there was almost nine times as many longs as shorts in the securities lending universe.

Graph 5

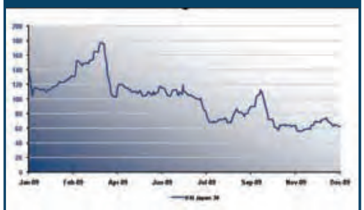


The market rally certainly put a damper on short selling, but so did the overall drop in leverage offered to hedge funds by banks and prime brokers. As we begin 2010 the big questions are, will the rally continue and will short sellers continue to sit on the market sidelines?

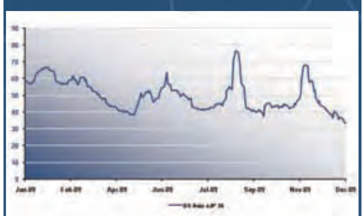
Graph 6 - DXI EU xUK 30



Graph 7 - DXI Japan 30



Graph 8 - DXI Asia xJP 30



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Spain

2009 was another interesting year for the securities finance industry in Spain. Despite representing a small part of overall securities lending activity, short selling and its relation to securities lending was a hot topic in the first quarter of the year in Spain as well as in the rest of Europe. Rights issues, scrip dividends and some merger and acquisitions opportunities have been driving most of the features we saw this year.

Securities lending activity during the year was fairly similar to the previous year, with new loans amounting to around 44.5mn shares. Volume was smaller, however, despite improvements in the main Spanish indices, amounting to EUR 440bn, against EUR 560bn in 2008.

Regulations

On the regulation side, the obligation to communicate any short selling on Spanish financial institutions above 0.25 per cent, released in 22nd of September 2008, remains in place. As we've already mentioned, short selling was highly discussed during the first quarter of the year, following 2008 events. Since then, disclosures on short selling activity have fallen dramatically as investors have changed from a directional view to a multi strategy type of activity.

On the investment fund side, we are still expecting the final law on securities lending for Spanish Asset Managers to be approved, after being delayed due to market conditions in 2008 and 2009. As financial markets recover, we hope to see the law released during 2010. As a reminder, key points are: (i) borrowers will need a minimum rating of A1, A+, (ii) only open trades with a maximum duration of one year, (iii) lending transactions should be covered by a guarantee with a market value of at least 105 per cent of the loan, (iv) at no time may the actual value of the securities lent exceed 75 per cent of the fund's net worth and (v) at no time may the actual value of the securities lent to one institution or to institutions belonging to the same group exceed 35 per cent of the fund's net worth.

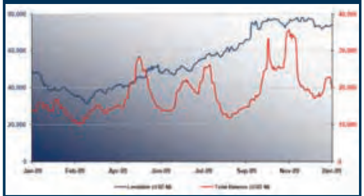
The opening of this market will not only allow access to a significant pool of both domestic and international assets, but it will also provide asset managers with an additional tool to improve their overall return on assets under management. Asset managers are key players of the securities lending activity and critical for market liquidity.

Significant Securities

As was the case last year, five names from the IBEX 35 - Santander, Telefónica, BBVA, Iberdrola and Repsol - represented more than 75 per cent of the overall securities lending activity, on the back of yield enhancement trades and corporate events. During 2009, many European companies cancelled or dramatically reduced their dividend payments and particular attention was paid to those still offering a good return to investors, with some Spanish companies amongst the most attractive in Europe.

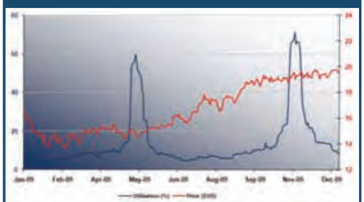
Like their European peers, Spanish companies have also begun to use scrip dividends as a way of remunerating shareholders, giving them the

Graph 1 - Spain Equity



Graph 2 - Ferrovial S.A.

Graph 3 - Telefónica SA



Graph 4 - Gestevisión Telecinco SA

Table 1

Asset Class	As at end December 2009		Group Average Results January to December 2009			
	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Spain Equity	73,624.60	20,199.60	21.02	119.59	25.34	28.36
ES Equity (IBEX)	71,597.40	19,688.40	21.00	112.26	24.19	27.17
ES Equity (IBEXC)	1,549.90	390.00	22.63	308.31	62.13	67.03
ES Equity (Others)	477.20	121.10	19.65	329.18	59.63	62.05
Spain Government Bonds	39,112.30	6,451.10	31.42	8.03	2.42	7.87
Spain Govt Bonds (Domestic)	34,151.70	5,943.20	33.46	8.07	2.60	8.26
Spain Govt Bonds (International)	4,960.60	507.90	16.70	8.64	1.11	5.07

opportunity to choose whether to receive dividends in new shares or in cash. Banco Santander and Iberdrola have offered shareholders this option and we expect more to do so during 2010.

Rights issues have been strongly used to raise cash during 2009. Gas Natural closed the largest rights issue of the year (to finance part of its acquisition of Union Fenosa). Iberdrola, NH Hotels, Pescanova and Jazztel are just some examples of companies that were active during the year. Low volumes and liquidity in some of those names impacted securities lending activity, as reflected in some of the graphs.
On corporate actions, Iberia's planned merger with British Airways, the above mentioned Gas Natural acquisition of Union Fenosa and the Ferrovial - Cintra merger have been the main drivers of securities lending activity in this area. Ferrovial also gathered a lot of interest on the back of BAA's obligation to sell some of its UK based airports due to UK Competition's concerns about its market dominance, at probably not the best market environment possible for such a transaction.

Outlook

To sum up, 2010 should be another hectic year. We expect an increase in both rights issues and scrip dividends, as well as M&A activity. It will be interesting to see the Committee of European Securities Regulators feedback on short selling recommendations for both transparency and harmonisation and how the market takes these into practice. We will hopefully see the addition of Spanish asset managers, adding more liquidity and supply to a market seeking it.

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Telefonica SA	ES Equity (IBEX)
2	Banco Santander SA	ES Equity (IBEX)
3	Banco Popular Espanol SA	ES Equity (IBEX)
4	Banco De Sabadell SA	ES Equity (IBEX)
5	Iberdrola SA	ES Equity (IBEX)
6	Repsol Ypf SA	ES Equity (IBEX)
7	Acs Actividades De Construccion Y Servicios SA	ES Equity (IBEX)
8	Banco Bilbao Vizcaya Argentaria S.A.	ES Equity (IBEX)
9	Industria De Diseno Textil Sa (Inditex SA)	ES Equity (IBEX)
10	Bankinter SA	ES Equity (IBEX)

General

From a Spanish standpoint, there is a Special Tax Regime that may be applicable for two types of securities loans in: (i) securities listed on a Spanish securities market exchange and (ii) securities listed on market exchanges and other organised markets (subject to certain conditions).

In general terms, the purpose of the borrowing must be to fulfil a sale order, for onward lending, to post as collateral in a financial transaction, or to participate in a corporate action (eg. rights issue).

Additionally, there are a number of other conditions to qualify as a stock loan, including the requirement to return equivalent securities, to make payments to the lender to deliver the economics rights (eg. income) from the securities, and the loan term should not exceed one year and be made or implemented with the involvement of certain Spanish financial institutions.

Spanish direct tax considerations

For a Spanish lender, no capital gain/loss would arise from the delivery or the repayment of the securities on loan. Fees received by the lender would be taxable as returns obtained on the assignment of capital at the general corporate rate of 30%. The borrower would be required to withhold on income paid to the lender, except where the lender is a credit institution registered with the Bank of Spain (Banco de España). If a credit institution was an intermediary in the security loan, the credit institution would be required to withhold.

For a resident borrower, income derived from securities borrowed would be taxed at the corporate rate of 30% as income derived from holdings in the equity (e.g. dividends). Manufactured dividends would be assessed as interest/financial expense, and would be tax deductible according to the Spanish Tax legislation.

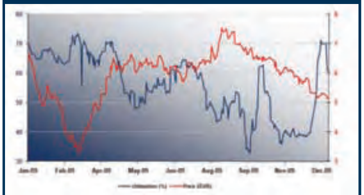
Other taxes and considerations

Both the transfer and the acquisition of securities by the borrower or the sale of borrowed securities, are exempt from Value Added Tax, Capital Duty and Stamp Duty Tax.

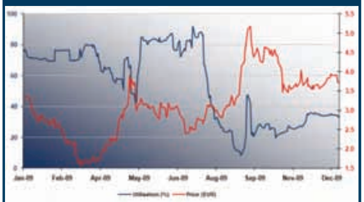
Based on information current as at 1 January 2010.

Deloitte.

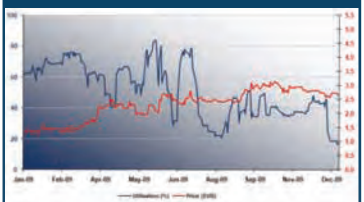
Graph 5 - Banco Popular Español SA



Graph 6 - NH Hoteles SA



Graph 7 - Jazztel PLC



Graph 8 - Pescanova SA

All graphs and tables have been sourced using the Data Explorers suite of products.

Santander Global Banking & Markets Spain

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United Kingdom

2009 was a rollercoaster ride of a year for the UK economy as the new year marked the official start of the worst recession since 1921. The year is scored with government intervention and stabilisation as the economy struggled to enter into the recovery phase. The UK is set to be the last major economy to exit recession. In securities lending, much remained the same – returns, utilissation and fees were all in line with 2008.

Market Analysis

Though lagging behind other markets with the exception of Spain, the UK has seen a positive increase in lendable assets over the past twelve months, contrary to the substantial fall observed in the previous year. The FTSE 100 saw its best annual performance since 1997 as it rose by 22% over the year while lendable assets increased by 31%. The rise in balances was mainly market driven but also there is evidence of growing confidence as lenders return to lending programmes.

Both UK equities and government bonds continue to have the largest lendable pool of assets compared to their European peers.

Returns are very similar to 2008 – equities earned 0.05bp more in 2009 whilst government bonds fell back 1.09bp. The move to higher SL fees and lower utilisations was far less marked in the UK than other European markets.

The FSA has been reviewing its short selling policy during 2009 and requires disclosure to the market of net short positions of 0.25% or more of the issued share capital of UK financial sector companies or companies carrying out a rights issue. The FSA is working closely with the Committee of European Securities Regulators (CESR) to ensure it adheres to a harmonised short selling disclosure regime as and when this is agreed.

Significant Securities

The British love affair with property has fallen apart in the last couple of years and it is not surprising to see a number of real estate companies feature in the top 10 list. Liberty International, British Land and Hammerson all were the subject of directional interest although British Land also attracts lending and borrowing interest as it pays four dividends a year.

Liberty topped the chart and saw utilisation of its securities reach 70% in early 2009 before falling back to below 50% by year end, still the 4th highest utilized security in the FTSE 100 at year-end.

British Land saw its short base (percentage of shares outstanding on loan) steadily decline over 2009 to 5%. Its utilisation averaged 26.8%, whilst the market averaged 8.2%, but it ended the year in a more upbeat position with rising valuations, a keen eye on Europe, increased share price and relatively low short interest.

It's been an interesting year for the HMV Group as it moved into the final year of its 3 year restructuring programme, acquiring a 50% stake in MAMA Group amidst rumours of the CEO moving to ITV plc, which were later quashed. Although it again underperformed the FTSE 100 and its share price halved, its short base has almost halved to 14.8% from 24% over the year. The average utilisation of 62.6% has been exceptionally higher than the mid-cap market average which is 17.4%. HMV Group has held on to build market share as others including Borders and Woolworths disappear from the scene.

Security of the Year

Heritage Oil outperformed the FTSE 100 in 2009 with gains of 140.72%, although overall performance during the year was mixed. Utilisation levels average 48.8% compared with a mid-cap market average of 17.44% as the stock was haunted by the deal of the year that never was. Heritage oil saw its short base (percentage of shares outstanding on loan) tumble to a confident 3.7% in July, from a peak of 7.8% as it entered talks with Kurdish Genel Energy over a reverse take-over which pumped the share price. Short base increased back to an average of 5% by the year end following termination of the proposed merger and new talks to sell out of Uganda discoveries. Heritage Oil's convertible bond also continues to drive borrowing interest.

Outlook

We anticipated a bumpy road for the UK market for 2009 but from a securities lending perspective the market has provided solid, consistent returns. The UK market may be more interesting than other European markets – with property recovering and banking over its worst, it will be interesting to see which sector takes the lead in 2010 and change in mix of significant securities from 2009.

The FSA has been supportive of securities lending and continues to work with international regulators to develop a harmonised approach to short selling disclosure – an approach that will be welcomed by practitioners as this should reduce costs associated with providing such disclosure.
– an approach that will be welcomed by practitioners as this should reduce costs associated with providing such disclosure.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
UK Equity	557,533.60	40,201.50	7.91	35.35	2.64	3.13
UK Equity (FTSE 100)	465,233.10	25,940.80	6.65	24.66	1.64	2.01
UK Equity (FTSE 250)	54,614.40	9,308.20	16.85	53.58	8.18	8.92
UK Equity (Others)	37,686.20	4,952.60	9.60	63.63	5.63	6.92
UK Government Bonds	227,170.10	111,086.60	55.40	9.30	5.15	7.78
UK Govt Bonds (I/L) (Domestic)	72,525.70	22,916.90	47.56	9.58	4.67	6.63
UK Govt Bonds (Non I/L) (Domestic)	154,010.30	88,121.10	58.73	9.23	5.36	8.26

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Liberty International Plc	UK Equity FTSE 100
2	Hsbc Holdings Plc	UK Equity FTSE 100
3	British Land Co Plc	UK Equity FTSE 100
4	Royal Dutch Shell Plc	UK Equity FTSE 100
5	Heritage Oil Ltd	UK Equity FTSE 250
6	Hmv Group Plc	UK Equity FTSE 250
7	Hammerson Plc	UK Equity FTSE 100
8	Standard Chartered Plc	UK Equity FTSE 100
9	Land Securities Group Plc	UK Equity FTSE 100
10	Prudential Plc	UK Equity FTSE 100

General

Generally under UK tax rules, full beneficial and legal ownership is transferred to enable the borrower to sell the securities and purchase replacement securities at a later date to fulfil its obligations. However, the lender retains economic ownership and should continue to recognise the securities in the financial statements.

UK direct tax considerations

As the title of the securities are transferred, dividends or interest would be received by the borrower. UK legislation provides that any capital gain that arises on the initial lending and the final transfer back to the lender (provided that the securities returned are in the same quantities and nominal value,) is disregarded for the purposes of Capital Gains Tax unless the lender requires the return to be paid in cash. In such a case the proceeds of redemptions would fall under the CGT legislation.

There are tax rules in place to prevent lenders from receiving a return from the borrowers in non taxable form and legislation in the event a borrower fails to return the securities. The legislation stipulates that where it becomes apparent that the borrower will fail to return the securities, the borrower is deemed for capital gains purposes as acquiring them at that time and the lender disposing of them at market value. Following the collapse of Lehman Brothers, an exception to this rule was included in legislation where default is due to the insolvency of the borrower and the lender uses collateral provided to acquire replacement securities.

Collateral from the borrower typically takes the form of cash or other securities. The UK has legislation in place to prevent agreements whereby no manufactured dividends are provided but instead replaced by interest income that has arisen on the collateral received. Further anti avoidance legislation is also in place to prevent the lender or borrower from substituting a non taxable or lowly taxed income in place of existing taxable income stream.

An important feature of the UK lending market is the complex Manufactured Overseas Dividends ('MOD') rules operated by the UK tax authorities ('HMRC'). The MOD regime regulates the securities lending industry and aims to put the UK lender of securities in the same position, from a tax perspective, as if the securities loan had not been made (i.e. tax neutrality). This tax neutral treatment is implemented via the imposition of a 'relevant withholding tax'. To facilitate the regime, financial intermediaries may assume, by application to HMRC, tax designations of Approved UK Intermediary ('AUKI') or Approved UK Collecting Agent ('AUKCA). Complex rules exist to enable the disapplication by AUKIs/AUKCAs of the relevant withholding tax.

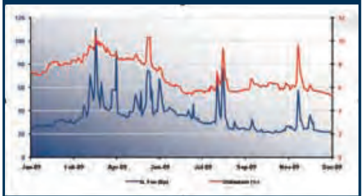
Other taxes and considerations

Relief from stamp duty and SDRT is available in respect of stock loans or recall where there is an arrangement for transfer and return of the same kind and amount of securities. An appropriate flag on the CREST system is used to effect this. Generally, the non-return of securities under a lending arrangement triggers SDRT on the borrower. In Finance Bill 2009, legislation was introduced to provide relief from taxes where one of the parties to a stock lending or repo arrangement becomes insolvent before the arrangement is completed by the return of the securities originally lent or sold. The relief applies to the recipient of the securities, covering any securities provided as collateral and subsequent purchases of securities by the solvent party to replace those not returned.

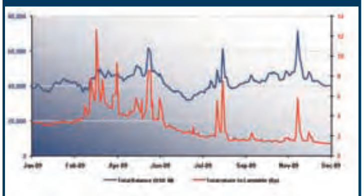
Based on information current as at 1 January 2010

Deloitte.

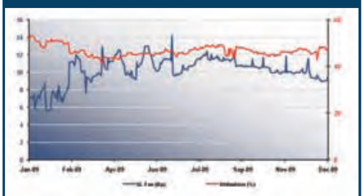
Graph 1 - UK Equity



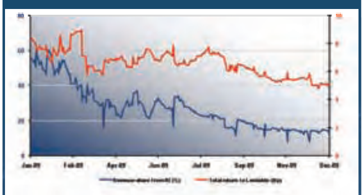
Graph 2 - UK Equity



Graph 3 - UK Government Bond



Graph 4 - UK Government Bond



Graph 5 - Security of the Year
Heritage Oil Limited

All graphs and tables have been sourced using the Data Explorers suite of products.

Data Explorers

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International Securities Lending Association Review of 2009

The Association has had an extremely active year on a number of fronts and highlights include a revised legal agreement, interactions with regulators, the development of a dialogue with beneficial owners, and the publication of several best practice papers. The following is a summary of the main events of 2009 and some consideration of what we expect 2010 might hold in store.

Beneficial Owners

In the early part of the year we continued to be very active in helping members deal with the issues raised during the credit crisis. Our publication "Securities Lending – Your Questions Answered" was designed to help beneficial owners understand more fully how the securities lending markets operate and what risks are involved and how these can be managed. During the year we held two forums for beneficial owners, one in Brussels and the other London (in conjunction with the IMN Beneficial Owners conference), in which we discussed subjects of interest to that community. We plan to make these forums a key part of our work schedule going forward.

Regulation

2009 saw a plethora of consultations on short selling. We are currently awaiting the feedback from CESR (The Committee of European Securities Regulators) on their consultation paper proposing a pan-European disclosure regime for short selling. Many domestic regulators are awaiting CESR's guidance and we are very hopeful that this will lead to a much greater degree of harmonisation across Europe at least. Given that a disclosure regime is likely we (along with AFME and ISDA) have been urging CESR to consider sensible thresholds for reporting, and to the extent that public disclosure is mandated that this be anonymous.

The focus on short selling and the general financial crisis has meant that there has been little in the way of new regulation in Europe that directly affects securities lending markets. One initiative worthy of mention is a study of securities lending recently undertaken by the UK FSA at the request of Lord Myners. We have been working very closely with the team involved who appear generally satisfied with the state of the market, but they have highlighted a small numbers of areas of concern and most notably would like to see more educational and informational material available for beneficial owners. We are in the process of establishing a working group comprising ourselves, the NAPF, IMA and ABI with the objective of producing a number of publications by mid-summer. The FSA and Bank of England will participate as observers.

Corporate Governance

Towards the end of last year we began working the International Corporate Governance Network (ICGN) with the objective of publishing a mutually agreed policy on corporate governance and securities lending. We plan to produce this by June 2010 to coincide with our respective annual conferences. We already have a good degree of agreement and will concentrate on resolving, or at least clarifying, those areas where we may have differing points of view. ISLA has already made it clear that it does not believe that borrowing stock with the primary objective of obtaining the vote is appropriate and indeed the GMSLA has been strengthened to reflect this view by making it a potential breach of contract to behave in such a fashion. The other area of debate will centre around the degree of transparency and reporting of stock loans.

Agent Lender Disclosure

The deadline for FSA regulated firms to comply with the regulatory capital requirements of Basel 2 was January 1st 2010. From this date borrowers need robust systems in place to report fully on their exposure to individual principals in agency programs. ISLA has provided a forum for members to co-ordinate their projects and has developed a model, closely based on that used in the US, which firms can use to exchange the vast amounts of data required. Early signs are that the market has performed well in the first few days of live production in 2010.

Operations

We have an extremely active and enthusiastic operations committee who continue to promote operational excellence and develop best practice standards for our business. At the point of writing this ISLA has published 8 best practice papers and more are in production. We are also in the process of rolling out the ISLA Automation Standard which will recognize individual firm's commitment to automating operational processes. Planning for our 2010 Operations Forum which is likely to be held in March is underway. Our 2009 event attracted 120 attendees.

GMSLA 2009 and GMSLA 2010 and Set-Off Protocol

Our new agreement was published in the summer however in response to a small number of queries from firms the ISLA Board agreed in December to make some minor changes to the document. The changes do not affect the set off provisions (which were developed from the experience of firms during the Lehman default) but relate to areas where the agreement did not necessarily reflect current market convention. The revised form of wording will be published in January following approval by the Board.

We then also expect to publish new guidance notes to the agreement and focus on getting the agreement and the ISLA Set-Off Protocol 2009 more widely adopted. There has been a lot of interest in the Protocol and many firms have confirmed that it is an attractive option. As a reminder, the Protocol enables firms to replace the provisions in their pre 2009 agreements that govern what happens following a default, with the relevant provisions of the GMSLA 2009.

Looking Ahead 2010

Things in the pipeline for 2010 include continuing focus on regulatory developments, education and our own conference. We expect to spend time analyzing the consequences of expected new regulations for short selling and other matters that that fall broadly under the headings of capital, liquidity and financial systemic risk management rules, all of which have the potential to affect our market. Over the past couple of years ISLA has organized a number of very successful educational workshops and forums. We have recently started to look at developing a more formal and structured approach to education and are considering what types of courses and materials could be produced and how these might be offered. And finally, following a very successful 2009 conference in Barcelona, we have agreed to hold another conference this year which will be in Berlin in June. More information on this (and most of things mentioned above) can be found on our website.

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SOCIETE GENERALE
Securities Services

Société Générale
Securities Services Liquidity Management

Optimize Your Asset Liquidity Through an Agent Lender

In light of the previous crisis, beneficial owners should evaluate the appropriateness of the route they have taken for Securities Lending. Basic principles are more relevant than ever: even the short term should be carefully contemplated and lending a massive part of one's inventory to a single counterparty under an exclusive arrangement is not necessarily a sound practice. All aspects of the risks involved in Securities Lending, such as liquidity, counterparty risk and operational risks, should be addressed. Risk management has become an increasingly important factor in the Securities Lending business. Beneficial owners are looking for better risk adjusted returns. As market events cause risk and fee levels to fluctuate, agent lenders must constantly monitor and adapt to changes. Lending through an agent provides many benefits in the current market conditions.

Although beneficial owners are free to set up an in-house operation, front and back-office functions, operational costs, financial capabilities, risk management and a regulatory framework can become obstacles in running a direct lending business profitably. Hence, the outsourcing of Securities Lending to an agent lender often makes more sense as it allows beneficial owners to better focus on their core business whilst benefiting from economies of scale, including investment in the information systems necessary to run such an activity.

Some lenders, such as Société Générale Securities Services, can provide not only agency lending programmes for clients with securities already held in custody by Société Générale, but may also act as a third-party agent for portfolios not in our custody. In the case of third-party lending, as for custodial lending, there is no disruption to the portfolio management from an availability point of view nor are relationships impacted with the non-SG securities custodian.

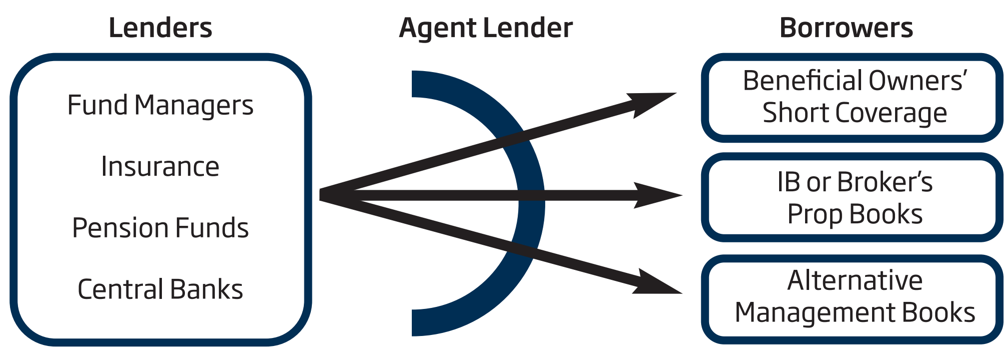
Advantages of Working with an Agent Lender

Value-added services: from custody to Securities Lending, pave the way for more seamless transaction processing. A comprehensive service provider offering a complete value chain has a better grasp of the overall process, is able to integrate different services efficiently and cost-effectively, can offer individualised programme enhancements, and include, if need be, some exclusives within the lending programmes. Via an agent, the beneficial owner gains a wider access to the market and increases the utilisation rate of their lendable inventory and consequently their return. Last but not least, beneficial owners can adjust their revenue profile to match their risk appetite. While an exclusive contract provides a secured income for beneficial owners, lending with a traditional agency programme (shared revenue) allows them to benefit from market opportunities.

Operational efficiency is an increasingly important contributor to overall fund performance. Responsibilities encompass keeping users up-to-date, processing and checking transactions, monitoring and allocating collateral, processing recalls and reallocation, coupon payment and corporate actions, allocation of lending revenues, and measuring exposures and risks. For large portfolios, the agent provides performance benchmarking for market levels.

Ensured compliance: Agent lenders have the market knowledge to enforce stringent rules, monitor counterparties and verify compliance both pre and post-trade. Indeed, Risks & Compliance are key parts of an agency lending programme. Its efficiency and areas of responsibilities have rapidly evolved over the past year to meet the demands of an increasingly sophisticated industry. Currently, compliance responsibilities encompass data controls, audits, tax compliance, investment vehicle monitoring, operational risk and information security.

Securities Lending Through an Agent Lender



Cash reinvestment: accepting cash as collateral is a way of achieving better utilization of the portfolio as borrowers may prefer this type of collateral. The reinvestment of cash can maximise further the portfolio revenues. The crisis has resulted in an enhanced focus on cash collateral and returns through the reinvestment of cash. Of course clients should be cautious about the quality of the instruments in which the cash is reinvested, thus requiring a diversified investment strategy on the lending agents' part.

The reinvestment process, as part of a lending programme, is tailored to customers' needs in terms of the size of cash reinvestment, risk profile and duration, and according to the agent lenders' assessment of investment suitability.

Risk knowledge: It is the agent lender's role to ensure that risks remain within clients' investment policies.

Risk management remains a key part of the Securities Lending business. Portfolio performance needs to be constantly weighed against risk. This is where the risk management expertise of the agent lender makes a difference. As illustrated by the crisis, two of the main risks encountered within the Securities Lending market are liquidity risk and counterparty risk. Both securities lenders and borrowers face liquidity risk. Market participants aim to avoid liquidity risk by increasing collateral quality and cash reinvestments within diversified liquid and/or short term instruments. Counterparty risk is mitigated through agency lending programmes by offering diversification and indemnification in case of counterparty default. The regular review of counterparty credit risk is important especially in the case of deterioration of the counterpart's financial situation or the specific situation of the market. When Securities Lending is carried out by a diversified banking institution, beneficial owners profit from a larger spectrum of risk analysis. Moreover, beneficial owners can leverage on the risk management of the Agent Lender. In this respect, and to guarantee objectivity, beneficial owners should ensure that the agent's risk management is performed by a dedicated team independently from the Securities Lending group.

Agency lending is an efficient way of lending portfolios addressing all related risks. It is an alternative for those beneficial owners who may not be satisfied with the direct exclusive arrangement (concentration of risk), although a part of the portfolios may be handled by the agent on an exclusive basis. Furthermore agency lending may be an appropriate way to reactivate Securities Lending for those who have suspended their activities in the past. Lending through an agent is also a good way of seizing additional and stable revenues from a greater number of borrowers.

At Société Générale Sécurities Services, our Liquidity Management experts offer a full range of flexible Securities Lending programmes which are tailored to each client's needs and built to boost portfolio performance. Backed by strong post trade support and reporting, we closely monitor collateral and rigorously benchmark our performance, while you remain in full control of your assets. Through our web site (www.sg-securities-services.com), SGSS provides a performance benchmarking programme including market analysis, comments on customer performance and real-time reporting.

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US Pension Funds have historically generated higher securities lending returns than US Mutual Funds - but at what cost?

Securities lending returns comprise two components. "Total Return to Lendable" is expressed as: -

securities lending (SL) return to lendable + reinvestment (RI) return to lendable = Total Return to Lendable

The scale, volatility and attribution of returns are important to anyone with responsibility for securities lending programme oversight.

They facilitate comparison of lending performance to your peers and inform conversations with management, boards or providers. They also provide excellent insight into the risks being taken.

Securities lending programmes vary - but due to regulatory guidance, historic inertia and a propensity to "crowd" many programmes have more in common with their peers than might at first be realised. However, some programmes have avoided recent problems and certain styles of lending have been vindicated.

We present the returns of the US Pension Funds (USPFs) and US Mutual Funds (USMTs) (source: Data Explorers) over the last 3 years. The USPFs consistently outperform the USMFs. This observation was made at the SEC Roundtable on Securities Lending by the author, Mark C Faulkner 29th September. A full transcript of the discussion can be read at: - http://www.sec.gov/news/openmeetings/2009/roundtable-transcript-092909.pdf.
Furthermore a greater proportion of the returns come from re-investment rather than "securities lending" itself.

Some argue that the USPF sector had historically engaged proportionately more in leverage finance than securities lending and that they have only now adopted a profile more in line with the USMF sector.

The mean return of the total return to lendable generated by the USPFs is almost double that of the USMFs over the period. The difference at the present time is now at its historic low and the USPFs have reigned in re-investment guidelines and reduced their return expectations.

The difference in volatility of total return is dramatic. The USPFs exhibit more than double the returns volatility of the USMFs. It is this higher volatility combined with the excess return that should have prompted those with compliance and fiduciary responsibilities to ask questions that may have altered their risk profile. It is easy to be wise after the event but for many their returns profile looked too good to be true – and it was.

This fact justifies the increased interest and vigilance that clients are showing in securities lending. This increase in oversight is one positive outcome from recent events.

Some believe the different returns reflect the different regulations governing each sector, others that it is due to the sophistication and level of engagement by those overseeing the programmes. Irrespective of the cause - this marked difference should have prompted questions and actions that could have prevented some USPFs (and their providers) getting into difficulty.

Graph 1 shows the mean securities lending return of the two sectors is broadly in line (5.29bp for the USMFs versus 6.0bp for the Pension Funds). However, the heightened volatility of the securities lending return generated by the USPFs (5.39bp Vs 2.6bp) is important when considering risk management.

Graph 2 shows the extent to which USPF return has come from "re-investment" rather than the "securities lending".

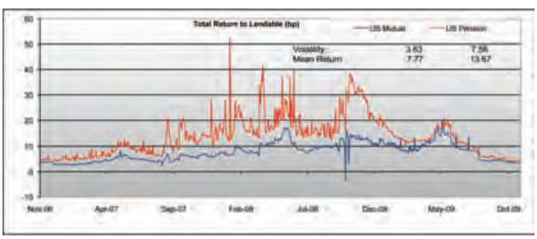
The re-investment return of the USPF Sector is three times that of the USMF Sector – with volatility along similar lines. Again, one can observe a more normal level of re-investment return today.

Conclusion

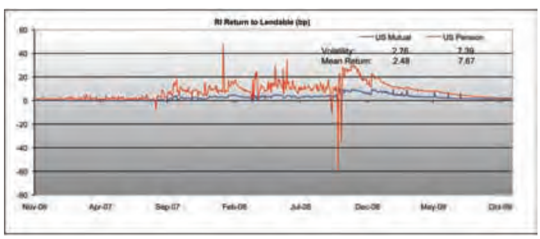
USPF securities lending returns have often dramatically exceeded those of the USMFs. These returns were more volatile and more dependent upon cash re-investment (96% of the collateral taken by US beneficial owners is USD - versus 25% in the UK and 20% in Canada).

This return profile was indicative of programmes that contained more risk which has recently manifested itself. Monitoring the scale, volatility and attribution of securities lending programme returns is a useful tool in the management of risk.

Graph 1



Graph 2



Other Securities Lending Markets

Depository Receipts

As we correctly speculated in the 2008 Yearbook, 2009 wasn't quite as good a year for holders of depository receipts, primarily due to most being lent versus cash collateral, the returns for which decreased significantly during the last 12 months. Pure lending fees held up and there are good returns to be made for holders of large cap names as well as emerging market depository receipts.

Market Analysis

Anyone taking a close look at the 2007 and 2008 Yearbooks will surmise that depository receipts are drifting back to pre-crunch levels and it is difficult to disagree. However, that would unfairly tarnish depository receipts which frankly mirror much activity going on elsewhere. After all, outside of the big European markets (ex-UK), returns don't get much more exciting than a TRTL of 10bp or so.

Assets available for lending have grown by nearly 60% since the end of 2008 and there have only been marginal shifts in the rest of the key numbers – utilisation has dipped, SL fees have popped slightly leaving the SLRTL (or the "rental" value of the loan) to fall less than 0.5bp. Reinvestment earnings are the big influence on a fall in TRTL as money market yields have declined.

For holders of ADRs, the earnings, whilst relatively ordinary, are a nice, sometimes unexpected, addition to their returns. After all, many assets have been bought because it has not been possible to purchase them in their domestic market or there has been a price opportunity over the domestically listed shares.

Significant Securities

As with 2008, there is a good mix of large cap and emerging market names in our top 10. The utilisation of the large cap names are driven by exactly the same reason as the interest in the domestic securities – dividend dates. However spikes are larger with average utilisation during those few days being around 80% compared to 60% for their domestic equivalent.

Not surprisingly, the large cap names are big dividend players – HSBC's four a year make it a popular security to borrow whilst Total and ENI offer two each.

The Israeli company, Teva Pharmaceutical, actually saw a significant reduction in interest during the year - its utilisation fell gradually through the year as its share price rose – it is unlikely that we will see this security feature in 2010 if the trend continues.

The excitement in this asset class is around the Chinese security names that feature. LDK Solar, our Security of the Year for two years still features but three other Chinese names join it in the top ten. With the exception of Shanda Interactive Entertainment, they are all linked to the growing solar power industry – an emerging business in an emerging market – all exciting stuff. The share prices of all four have risen dramatically in 2009 and utilisations have followed as borrowers seek exposure to these new technology representatives. Utilisation of the three new names all rose from in the region of 40% to between 80 and 90% - if you held these securities in 2009 you were likely to get them out on loan and earn average returns of 5-6% with peaks of between 12 and 20% - not a bad reason to buy them in the first place particularly when share prices have moved upwards too.

Security of the Year

We looked hard to see if we could avoid giving LDK Solar the title for the third year running but gave up when we saw the returns that lenders had made. Since April, lending returns have been in the region of 20% giving average annual fees of over 15%. We have commented in previous years that asset holders would have also seen significant price volatility and 2009 was no exception – the share price bounced from USD 4 to USD 14 before ending the year at USD 7, still substantially off its 2008 peak.

As other emerging market names start to appear maybe there is a chance that LDK Solar will be usurped in 2010 although we doubt it.

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
Depository Receipts	169,773.70	28,137.30	12.68	78.15	6.43	9.89
American Depository Receipts	140,212.50	24,634.70	13.54	76.20	6.39	10.17
Global Depository Receipts	15,442.40	2,190.90	9.02	76.72	7.19	8.93
Other Depository Receipts	14,118.80	1,311.70	7.35	119.61	6.36	8.07

Outlook

Overall returns will probably continue drifting downwards but investors wishing to get exposure to new technology companies in today's emerging markets could do worse than buy some ADRs – securities lending returns in some companies are stellar – in this case maybe the tail does wag the dog!

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Total Fina Elf Adr	FR ADR
2	Nokia Adr	FI ADR
3	Ldk Solar Adr Repstg One Ord	CN ADR
4	Shanda Interactive Ent Adr	CN ADR
5	Suntech Power Hldng Adr Rptg One Ord	CN ADR
6	Yingli Grn Egy Hldg Adr Repg One Ord	CN ADR
7	Sanofi Aventis Adr Rep 1 1/2 Ord	FR ADR
8	Eni Adr	IT ADR
9	Teva Pharm Adr	IL ADR
10	Hsbc Holdings Adr	UK ADR

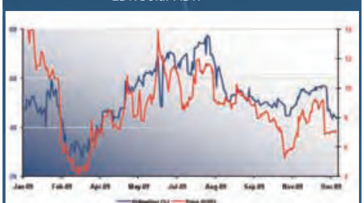
Graph 1 - Depository Receipts

Graph 2 - American Depository Receipts

Graph 3 - Global Depository Receipts

Graph 4 - Other Depository Receipts

Graph 5 - Security of the Year
LDK Solar ADR



All graphs and tables have been sourced using the Data Explorers suite of products.

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Exchange Traded Funds

Market Summary

After a slight dip in 2008 the global ETF market came back in 2009 to hit record asset levels. According to the Global ETF Research & Implementation Strategy Team at BlackRock, the US ETF assets hit an all time high of US 705bn in December 2009, while European ETF assets hit an all time high of US 223bn.

The traditional securities lending market for US ETFs has not followed the same trend as the cash market, we saw a marked increase in demand and supply for European ETFs. Could 2010 be the year that securities lending in European ETFs really takes off?

Market Analysis

US ETFs

The overall value on loan from the traditional securities lending market was relatively flat for the year (Graph 1) and the total number of ETFs with loan value was also fairly consistent for the year (Graph 2).

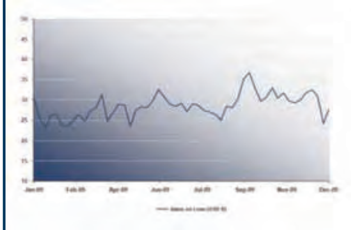
The value of lendable US ETF assets on the other hand saw a steady increase from the March 2009 lows (Graph 3) while the number of ETFs that were made available for borrow increased 7% to a total of 757 in December (Graph 4).

The top ten names that had the highest average value on loan was little changed from 2008. The Spdr Trust Etf, iShares Russell 2000 and Powershares QQQQ continued to have highest average demand (see table 1). The iShares family of ETFs also continued to dominate, with six iShares ETFs in the Top Ten.

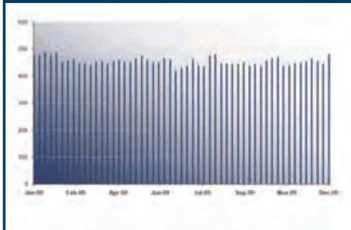
Table 1 - Top Ten US ETFs by Average Loan Balance

Name	Average Total Balance (USD m)	Average Utilisation (%)
Spdr Trust Etf	8,561	37.90
iShares Russell 2000 Index Fund	2,583	77.18
Powershares Qqq Trust Series 1	1,659	50.73
iShares Msci Eafe Index Fund	1,232	31.74
iShares Msci Emerging Markets Index Fund	1,156	32.35
iShares Dow Jones Us Real Estate Index Fund	988	89.85
iShares Russell 3000 Index Fund	866	24.65
Select Sector Energy Select Sector Spdr Fund	655	80.14
Select Sector Financial Select Sector Spdr Fund	596	51.92
iShares Msci Brazil Index Fund	561	43.75

Graph 1 - US ETF Value on Loan



Graph 2 - Number of US ETF with Loan Value



Graph 3 - US ETFs Lendable Value

Graph 4 - Number of ETFs with Lendable Value

European ETFs

In contrast to the US ETF traditional securities lending market, the demand for European ETF loans more than doubled over the course of 2009 (Graph 5). The number of European ETFs out on loan also doubled, with more than 300 out on loan by the end of the year (Graph 6).

After an initial spike in lendable value in February the overall value of European ETF made available to borrow drifted lower for most of the year (Graph 7). However, at the end of the year we saw new ETFs being made available. Graph 8 shows that the overall number of European ETFs that were made available to borrow in 2009 increased from 202 to just over 300.

The dominance of iShares in the top ten names that had the highest average value on loan continued in Europe (table 2). The iShares Ftse 250 ETF had the highest average balance with an average utilisation of over 50%.

Table 2 - Top Ten European ETFs by Average Loan Balance

Name	Average Total Balance (USD m)	Average Utilisation (%)
iShares Ftse 250 Gbp	79	52.26
Lyxor Etf Dj Euro Stoxx 50 Etf	43	25.99
Db X-Trackers Msci Usa Trn Index Etf	41	79.30
iShares Ftse 100 Gbp	40	5.87
iShares Dax (De)	34	28.04
iShares Dj Euro Stoxx 50 (De)	23	24.26
iShares S&P 500 Usd	21	10.47
Lyxor Etf Cac 40	20	26.85
Xact Omxs30	20	64.65
iShares Dj Euro Stoxx 50 Eur	18	27.85

Graph 5 - European ETF Value on Loan

Graph 6 - Number of European ETFs with Loan Value

Graph 7 - European ETF Lendable Value

Graph 8 - Number of European ETFs with Lendable Value

All graphs and tables have been sourced using the Data Explorers suite of products.

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South Africa

Market Summary For 2009

Emerging market equity investment inflows surged to record levels after the collapse of these markets during the credit crisis. After plummeting 46% from its 2008 high, the JSE All Share index subsequently surged 52% from its lows in March 2009. In addition, the South African (SA) Reserve Bank cut interest rates by 5% during the course of the year. The SA Rand (ZAR) appreciated sustainably with increasing inflows owing to elevated demand for SA's natural resources from countries with high incremental demand for raw materials, such as China and Brazil.

It's estimated that stock loan balances of JSE listed equities lent out by SA resident lenders decreased by 55% from the previous year high.

Influences And Drivers Of Performance

Due to market dynamics and conditions mentioned above, the drivers and demand for the borrowing of SA equities materially changed compared to the last few years, largely contributing to a reduction of short selling, hedging and defensive derivative structure appetite.

Unsurprisingly, given the economic backdrop, there was a dramatic fall in merger and acquisition (M&A) volume. This was predominantly caused by a lack of confidence in the overall environment combined with the reduced availability of funding. One of the main talking points revolved around MTN Group and the possible tie-up with one of the Indian operators. While a deal was never consummated the market continues to observe this space going into 2010.

Reviewing the SA banking sector, the first quarter saw the bulk of stock lending activities for the year which we believe was mostly driven by large international hedge funds. (Graphs 1 and 2). Having avoided much of the subprime crisis with limited impact from the international funding issues faced by banks in other regions, SA banks enjoyed a safe haven status for much of the second half of 2008 with global emerging market investors. However, the first quarter of 2009 brought with it early signs of a weakening macro environment, consumer spending strained by high rates as well as bouts of job losses. This set a tough backdrop for the SA banking sector, lending weight to shorting of SA bank stocks on a fundamental basis.

Borrow demand for Telkom SA (Graph 3) and Vodacom Group (Graph 4) was prevalent during the unbundling period of Telkom's 35% stake in Vodacom. Vodacom floated on the JSE in May, one of the biggest listings on the bourse in years.

The ruling African National Congress (ANC) political party won its fourth straight election victory since the end of apartheid, slightly short of the two-thirds majority needed to change the constitution. The party's controversial leader Jacob Zuma became the President. Zuma broadly managed to preserve a delicate balance between the ascendant left and market-friendly centrists within the ANC over the course of 2009, suggesting that he is well aware of the risks associated with spooking international investors with a deviation from market-oriented economic policies. However, it is noteworthy that when the dust settles further on a global scale and the international community starts to differentiate markets according to their fundamentals, any frailties seen in SA politics, may raise the country's risk premium in the future.

Trends And Developments

In a challenging stock lending environment such as 2009, equity finance/stock loan businesses in SA have seeked to diversify product and revenue streams, especially as opportunities arise for those businesses with financial strength post the credit crisis. For example HSBC launched its SA Synthetic DMA platform and expanded its Market Access product to countries such as Nigeria, targeting the increasing investor interest in the African continent.

With reference to M&A in SA, the market generally predicts a pick up from 2009 as general confidence grows, especially in the banking sector, allowing lending constraints to be relaxed. One would expect to see increased equity issuance both from M&A considerations as well as balance sheet recapitalisations. Africa remains on the agenda for several of the large telecoms operators. In addition, the more cash constrained companies in the consumer sector could open themselves up to consolidation.

SA will host the football World Cup in June 2010 offering the perfect opportunity to showcase the country as a viable investment haven and improve investor sentiment. According to research performed by HSBC, historically, holding the World Cup has little impact on GDP but the host's stock market almost always outperforms in the first half of the year.

Security Of The Year

Dual listed Liberty International (Graph 5) had two rights issues in 2009; in April to raise USD 1.08bn in an attempt to avert a breach in lending covenants and again in September, this time to fund income-maintenance projects and new acquisitions.

Deal Impact:

- Directional shorting: speculative and opportunistic shorting due to price-dilutive effects
- Cross border plays/arbitrage opportunities
- Recalls: lenders selling their long positions exacerbating demand and causing a spike in fees

Table 1

	As at end December 2009		Group Average Results January to December 2009			
Asset Class	Lendable Assets (USD m)	Total Balance (USD m)	Utilisation (%)	SL Fee (bp)	Securities Lending Return to Lendable (bp)	Total Return to Lendable (bp)
South Africa Equity	**21,626.40**	**1,982.30**	**3.82**	**46.05**	**1.58**	**2.14**
South Africa Equity (JSE40)	18,084.10	1,509.30	3.94	44.54	1.63	2.23
South Africa Equity (Others)	3,542.30	473.10	3.11	52.76	1.24	1.63
South Africa Government Bonds	**2,405.70**	**744.60**	**24.34**	**15.65**	**4.39**	**7.95**

Table 2 - Security Rankings by Total Daily Return

Rank	Stock Description	Security Type
1	Gold Fields Limited	ZA Equity (JSE40)
2	Nedbank Group	ZA Equity (JSE40)
3	Mondi Ltd	ZA Equity (JSE40)
4	Standard Bank Group	ZA Equity (JSE40)
5	Steinhoff International Holdings	ZA Equity (JSE40)
6	Bhp Billiton Plc	ZA Equity (JSE40)
7	Anglo Platinum Ltd	ZA Equity (JSE40)
8	Absa Group Ltd	ZA Equity (JSE40)
9	Netcare Ltd	ZA Equity (Others)
10	Anglogold Ashanti Ltd	ZA Equity (JSE40)

Notes:

1. Performance Explorer may not have captured many SA domiciled lenders' and as such the lendable asset base and total balances of SA securities could be far greater than shown in the graphs.
2. Some Charts and graphs may show greater figures for balance on loan than lendable assets – the reason for this is that there may be borrowers contributing data to the Performance Explorer database borrowing assets from lenders who do not contribute data to the system.
3. HSBC Africa would not claim to be able to cover all grounds behind the SA stock loan drivers in 2009; however we discuss a few highlights and elements worth noting.

General

Information around the taxation of securities lending arrangements was last issued by the South African Revenue Service ('SARS') during 1999, in the form of SARS Practice Note 5. However, since then, numerous amendments to the tax treatment of securities lending arrangements have been effected which render that Practice Note largely inappropriate. Further, SARS are presently reviewing the taxation of some aspects of securities lending arrangements.

South African direct tax considerations

Payments made by the borrower to the lender as a "manufactured dividend" is not a dividend for Income Tax purposes and will constitute gross income in the hands of the lender. For non-resident lenders, protection under an applicable tax treaty may be available where there is no permanent establishment in South Africa. The deductibility of the "manufactured dividend" paid depends on general principles. Manufactured interest payments are treated as interest for South African tax purposes.

Where the securities lent constitutes 'qualifying securities' loaned under a 'lending arrangement' (where shares are returned within a 12 month period), it is deemed not to be disposal in the hands of the lender.

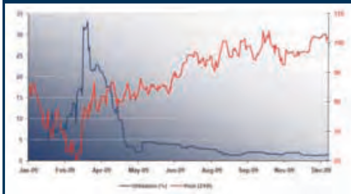
Other taxes and considerations

A fee or commission charged by a venture for making scrip available to another person is subject to VAT. The view is however, that a 'manufactured dividend' or 'manufactured interest' payment constitutes consideration for the supply of a financial service, and is exempt from VAT.

Securities transfer tax should not apply for the transfer of a security from lender to a borrower (or vice versa) under a lending arrangement which meets the relevant conditions.

Based on information current as at 1 January 2010

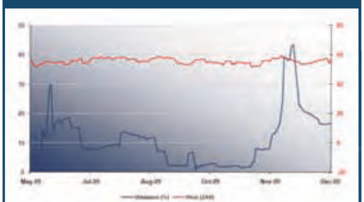
Graph 1 - Standard Bank Group Limited



Graph 2 - Nedbank Group Limited

Graph 3 - Telkom SA Limited

Graph 4 - Vodacom Group Proprietary Limited



Graph 5 - Security of the Year

Liberty International PLC

All graphs and tables have been sourced using the Data Explorers suite of products.

HSBC AFRICA

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Data Explorers - A Brief Introduction

Data Explorers is a rapidly expanding firm with headquarters in London and New York.

Over 3m daily transactions directly sourced from global securities lending desks

Data Explorers, based in New York and London, is the world's most complete resource for data, analytics and insight into short-selling and securities financing. Its unique data set of more than three million daily transactions is sourced directly from the securities lending desks of the world's top Investment Banks. By analyzing fund flow, stock loan availability, short interest, and stock lending volume, Data Explorers anticipates sector and security movements.

Since its launch in 2002, Data Explorers has brought transparency to investors in opaque markets, delivering real-time risk return analysis and informing better decision making across all segments. We are the go-to source for Investment Managers, Securities Lending Practitioners and Sell Side Professionals – offering the fastest, most reliable and comprehensive global short-side intelligence available.

Thought Leadership

Data Explorers is the key source for media coverage of securities lending and short interest, and we are actively working with regulators around the world to promote greater understanding of the role of the securities financing in the global financial system.

Our global Securities Financing forums and educational webinars offer innovative and creative programs designed to elicit intelligent industry debates and broaden understanding of the industry.

Please visit **http://www.dataexplorers.com/consulting-events** to learn more about our upcoming regional events and webinars.

Securities Lending Conference and Forums 2010

ASSOCIATION / INSTITUTION / COMPANY	DATE	VENUE
16th Annual Beneficial Owners' Summit on Domestic & International Securities Lending & Repo	7-10 February 2010	Four Seasons Aviara Resort, San Diego
7th Annual PASLA/RMA Conference on Asian Securities Lending	2-4 March 2010	JW Marriott Hotel, Pacific Place, Hong Kong
Data Explorers Securities Financing Forum	17 March 2010	Kings Place, London
Data Explorers Securities Financing Forum	26 May 2010	Four Seasons Hotel, New York
19th Annual ISLA/RMA Conference on International Securities Lending	22-24 June 2010	Adlon Kempinski, Berlin, Germany
Data Explorers Securities Financing Forum	29 September 2010	Hong Kong (venue to be confirmed)
IMN – 15th Annual European Securities Lending and Repo Summit	Autumn 2010	Europe (venue to be confirmed)
27th Annual RMA Conference on Securities Lending	11-14 October 2010	Boca Raton Resort & Club, Florida
Data Explorers Securities Financing Forum	17 November 2010	Madinat Jumeirah, Dubai

Glossary of Terms

Every industry has its own business terms. Securities lending is no exception. Here we list the more esoteric terms mentioned in this booklet and some that might be encountered whilst exploring the market. Note that some terms may have different meanings in contexts other than securities lending.

Accrued interest:
Coupon interest that is earned on a bond from the last coupon date to the present date.

Agent:
A party to a loan transaction that acts on behalf of a client. The agent typically does not take in risk in a transaction. See "Indemnity."

All-in dividend:
The sum of the manufactured dividend plus the fee to be paid by the borrower to the lender, expressed as a percentage of the dividend of the stock on loan.

All-in price:
Market price of a bond, plus accrued interest. Generally rounded to the nearest 0.01. Also known as "dirty price".

American Depositary Receipt (ADR):
Negotiable certificate issued by a U.S. bank representing a specified number of shares (or one share) in a foreign stock that is traded on a U.S. exchange.

Basis point (bp):
One one-hundredth of a percent or 0.01%.

Bearer securities:
Securities that are not registered to any particular party and hence are payable to the party that is in possession of them.

Beneficial owner:
A party that is entitled to the rights of ownership of property. In the context of securities, the term is usually used to distinguish this party from the registered holder (a nominee, for example) that holds the securities for the beneficial owner.

Benefit:
Any entitlement due to a stock or shareholder as a result of purchasing or holding securities, including the right to any dividend, rights issue, scrip issue, etc. made by the issuer. In the case of loaned securities or collateral, benefits are passed back to the lender or borrower (as appropriate), usually by way of a manufactured dividend or the return of equivalent securities or collateral.

BMA:
The Bond Market Association – is a US-based industry organisation of participants involved in certain sectors of the bond markets. The BMA establishes non-binding standards of business conduct in the US fixed-income securities markets. Formerly known as the Public Securities Association or PSA.

BRIC:
An acronym for the economies of Brazil, Russia, India and China combined.

Buy-in:
The practice whereby a lender of securities enters the open market to buy securities to replace those that have not been returned by a borrower. Strict market practices govern buy-ins. Buy-ins may be enforced by market authorities in some jurisdictions.

Buy/Sell,Sell/Buy:
Types of bond transactions that, in economic substance, replicate reverse repos, and repos respectively. These transactions consist of a purchase (or sale) of a security versus cash with a forward commitment to sell back (or buy back) the securities. Used as an alternative to repos/reverses.

BVI:
The German Association of Investment Companies

Carry:
Difference between interest return on securities held and financing costs:

Negative carry:
Net cost incurred when financing cost exceeds yield on securities that are being financed.

Positive carry:
Net gain earned when financing cost is less than yield on financed securities.

Cash-orientated repo:
Transaction motivated by the need of one party to invest cash and the need of the other to borrow. See also 'Securities-orientated repo'.

Cash trade:
A non-financing purchase or sale of securities.

Clear:
To complete a trade, i.e. when the seller delivers securities and the buyer delivers funds in correct form. A trade fails when proper delivery requirements are not satisfied.

Close-out (and) netting:
An arrangement to settle all existing obligations to and claims on a counterpart falling under that arrangement by one single net payment, immediately upon the occurrence of a defined event of default.

Collateral:
Securities or cash delivered by a borrower to a lender to support a loan of securities or cash.

Contract for Differences (CFD):
An OTC derivative transaction that enables one party to gain economic exposure to the price movement of a security (bull or bear). Writers of CFDs hedge by taking positions in the underlying securities, making efficient securities financing or borrowing key.

Corporate action:
A corporate event in relation to which the holder of the security must or may make an election or take some other action in order to secure its entitlement and/or to opt for a particular form of entitlement (see also equivalent).

Corporate event:
An event in relation to a security as a result of which the holder will or may become entitled to:
- a benefit (dividend, rights issue etc.); or
- securities other than those which he held prior to that event (takeover offer, scheme of arrangement, conversion, redemption, etc). This type of corporate event is also known as a stock situation.

Conduit borrower:
See intermediary.

CSD:
Central Securities Depository

Custodian:
An entity that holds securities of any type for investors, effecting receipts and deliveries, and supplying appropriate reporting.

Daylight exposure:
The period in the day when one party to a trade has a temporary credit exposure to the other due to one party having settled before the other. It would normally mean that the loan had settled but the delivery of collateral would settle at a later time (although there would also be exposure if settlement happened in reverse). The period extends from the point of settlement of the first side of the trade to the time of settlement of the other. It occurs because the two sides of the trade are not linked in many settlement systems or settlement of loan and collateral take place in different systems, possibly in different time zones.

Deliver-out repo:
"Standard" two-party repo, where the party receiving cash delivers bonds to the cash provider.

Delivery-by-value (DBV):
A mechanism in some settlement systems (including CREST) whereby a member may borrow or lend cash overnight against collateral. The system automatically selects and delivers collateral securities, meeting pre-determined criteria to the value of the cash (plus a margin) from the account of the cash borrower to the account of the cash lender and reverses the transaction the following morning.

Distributions:
Entitlements arising on securities that are loaned out, e.g. dividends, interest, and non-cash distributions.

DVP (Delivery versus payment):
The simultaneous delivery of securities against the payment of funds within a securities settlement system.

EEA:
European Economic Area

ERISA:
The Employee Retirement Income Security Act, a US law governing private US pension plan activity, introduced in 1974 and amended in 1981 to permit plans to lend securities in accordance with specific guidelines.

Equivalent (securities or collateral):
A term meaning that the securities or collateral returned must be of an identical type, nominal value, description and amount to those originally provided. If, during the term of a loan, there is a corporate action in relation to loaned securities, the lender is normally entitled to specify at that time the form in which he wishes to receive equivalent securities or collateral on termination of the loan. The legal agreement will also specify the form in which equivalent securities or collateral are to be returned in the case of other corporate events.

Escrow:
See Tri Party

Exchange Traded Fund (ETF):
A security that tracks an index, a commodity or a basket of assets like an index fund, but trades like a stock on an exchange, thus experiencing price changes throughout the day as it is bought and sold.

Fail:
The failure to deliver cash or collateral in time for the settlement of a transaction.

Free-of-payment delivery:
Delivery of securities with no corresponding payment of funds.

G7:
The Group of Seven, i.e. US, France, Japan, United Kingdom, Germany, Italy and Canada

G10:
The Group of Ten, i.e. US, France, Japan, United Kingdom, Germany, Italy and Canada, the Netherlands, Sweden and Switzerland

General Collateral (GC):
Securities that are not "special" (see below) in the market and may be used, typically, to collateralise cash borrowings. Also known as "stock collateral".

Gilt-Edged Securities (Gilts):
United Kingdom government bonds.

Gilt-Edged Securities Lending Agreement (GESLA):
See Master Gilt Edged Securities Lending Agreement.

Global Master Securities Lending Agreement (GMSLA):
The Global Master Securities Lending Agreement has been developed as a market standard for securities lending of bonds and equities internationally. It was drafted with a view to compliance with English law.

Gross-paying securities:
Securities on which interest or other distributions are paid without any taxes being withheld.

Haircut:
Initial margin on a repo transaction. Generally expressed as a percentage of the market price.

Hedge fund:
A leveraged investment fund that engages in trading and hedging strategies, frequently using leverage.

Hot/hard stock:
A particular security that is in high demand in relation to its availability in the market and is thus relatively expensive or difficult to borrow.

Hold in custody:
An arrangement under which securities are not physically delivered to the borrower (lender) but are simply segregated by the lender in an internal customer account.

Icing/putting stock on hold:
The practice whereby a lender holds securities at a borrower's request in anticipation of that borrower taking delivery.

Indemnity:
A form of guarantee or insurance, frequently offered by agents. Terms vary significantly and the value of the indemnity does also.

Initial Public Offering (IPO):
The first sale of stock by a private company to the public

Interdealer broker:
Agent or intermediary that is paid a commission to bring buyers and sellers together. The broker's commission may be paid either by the initiator of the transaction or by both counterparts.

Intermediary:
A party that borrows a security in order to on-deliver it to a client, rather than borrowing it for its own in-house needs. Also known as a conduit borrower.

International Securities Lending Association (ISLA):
A trade association for securities lending market practitioners.

Initial Public Offering (IPO):
The first sale of stock by a private company to the public

IOSCO:
International Organization of Securities Commission

ISMA:
The Zurich-based International Securities Market Association is the self-regulatory organisation and trade association for the international securities market. ISMA sets standards of business conduct in the global securities markets, advises regulators on market practices and provides educational opportunities for market participants.

Lendable:
The total value of holdings, in USD millions.

London Investment Banking Association (LIBA):
The principal trade association in the UK for firms active in the investment banking and securities industry. LIBA members are generally borrowers and intermediaries in the stock lending market.

M&A:
Merger and acquisition.

Manufactured dividends:
When securities that have been lent out pay a cash dividend, the borrower of the securities is in general contractually required to pass the distribution back to the lender of the securities. This payment "pass-through" is known as a manufactured dividend.

Margin, initial:
Refers to the excess of cash over securities or securities over cash in a repo/reverse repo, sell/buy-buy/sell, or securities lending transaction. One party may require an initial margin due to the perceived credit risk of the counterpart.

Margin, variation:
Once a repo or securities lending transaction has settled, the variation margin refers to the band within which the value of the security used as collateral may fluctuate before triggering a margin call. Variation margin may be expressed either in percentage or absolute currency terms.

Margin call:
A request by one party in a transaction for the initial margin to be reinstated or to restore the original cash/securities ratio to parity.

Mark-to-market:
The act of revaluing the securities collateral in a repo or securities lending transaction to current market values. Standard practice is to mark to market daily.

Market value:
The value of loan securities or collateral as determined using the last (or latest available) sale price on the principal exchange where the instrument was traded or, if not so traded, using the most recent bid or offered prices.

Master Equity and Fixed Interest Stock Lending Agreement (MEFISLA):
This was developed as a market standard agreement under English law for stock lending prior to the creation of the Global Master Securities Lending Agreement. It has a legal opinion from Queen's Counsel and has been mainly, but not exclusively, used for lending UK securities excluding gilts.

Master Gilt Edged Stock Lending Agreement (GESLA):
The Agreement was developed as a market standard exclusively for lending UK gilt-edged securities. It was drafted with a view to complying with English law and has a legal opinion from Queen's Counsel.

Matched/Mismatched book:
Refers to the interest rate arbitrage book that a repo trader may run. By matching or mismatching maturities, rates, currencies, or margins, the repo trader takes market risk in search of returns.

MBS:
Mortgaged backed securities.

Net paying securities:
Securities on which interest or other distributions are paid net of withholding taxes.

Off-the-runs:
All Treasury Bonds and notes issued before the most recently issued bond or note of a particular maturity. These are the opposite of "on the run treasuries".

On-the-runs:
The most recently issued U.S. Treasury bond or note of a particular maturity. These are the opposite of "off the run securities".

Open transactions:
Trades done with no fixed maturity date.

Overseas Securities Lenders' Agreement (OSLA):
The Agreement was developed as a market standard for stock lending prior to the creation of the Global Master Securities Lending Agreement. It was drafted with a view to complying with English law and has a legal opinion from Queen's Counsel. Intended for use by UK-based parties lending overseas securities (i.e. excluding UK securities and gilts), it has since become the most widely used global master agreement.

Pair off:
The netting of cash and securities in the settlement of two trades in the same security for the same value date. Pairing off allows for settlement of net differences.

Partialling:
Market practice or a specific agreement between counterparts that allows a part-delivery against an obligation to deliver securities.

Pay-for-hold:
The practice of paying a fee to the lender to hold securities for a particular borrower until the borrower is able to take delivery.

Prime brokerage:
A service offered to clients – typically hedge funds – by investment banks to support their trading, investment and hedging activities. The service consists of clearing, custody, securities lending, and financing arrangements.

Principal:
A party to a loan transaction that acts on its own behalf or substitutes its own risk for that of its client when trading.

Proprietary trading:
Trading activity conducted by an investment bank for its own account rather than for its clients.

PSA Public Securities Association:
The former name of the BMA.

Rebate rate:
The interest paid on the cash side of securities lending transactions. A rebate rate of interest implies a fee for the loan of securities and is therefore regarded as a discounted rate of interest.

Recall:
A request by a lender for the return of securities from a borrower.

Repo:
Transaction whereby one party sells securities to another party and agrees to repurchase the securities at a future date at a fixed price.

Repo rate:
The interest rate paid on the cash side of a repo/reverse transaction.

Repo (or reverse) to maturity:
A repo or reverse repo that matures on the maturity date of the security being traded.

Repricing:
Occurs when the market value of a security in a repo or securities lending transaction changes and the parties to the transaction agree to adjust the amount of securities or cash in a transaction to the correct margin level.

Return:
Occurs when the borrower of securities returns them to the lender.

Revaluation ("reval"):
See Repricing.

Reverse Repo:
Transaction whereby one party purchases securities from another party and agrees to resell the securities at a future date at a fixed price.

RI Return:
The revenue from reinvestment activity.

Roll:
To renew a trade at its maturity.

SBL:
Securities lending and borrowing

Securities-orientated repo trade:
Transaction motivated by the desire of one counterpart to borrow securities and of the other to lend them. See also Cash-orientated repo trade.

Securities Rankings Tables:
Within the market commentaries there are Security Rankings showing the top 10 securities per market. We assessed each market on an individual basis and used the following methodology- We calculated the top ten securities for the specific market ranked by Group Average Total Daily Return (absolute figures).

Shaping:
A practice whereby delivery of a large amount of a security may be made in several smaller blocks so as to reduce the potential consequences of a fail. May be especially useful where partialling is not acceptable.
Securities Lending Return to Lendable (SLRTL): The revenue from securities lending, scaled by the lendable assets, in Basis Points.

SL Fee:
The weighted average intrinsic securities lending fee of the loans the group has in the security category, in Basis Points.

Specials:
Securities that for several reasons are sought after in the market by borrowers. Holders of special securities will be able to earn incremental income on the securities by lending them out via repo, sell/buy, or securities lending transactions.

Spot:
Standard non-dollar repo settlement two business days forward. This is a money market convention.

Stock situation:
See corporate event.

Substitution:
The practice in which a lender of general collateral recalls securities from a borrower and replaces them with other securities of the same value.

TBMA/ISMA Global Master Repurchase Agreement (GMRA):
The market-standard document used for repo trading. The GMRA, whose original November 1992 version was based on the PSA Master Repurchase Agreement, was revised in November 1995 and again in October 2000.

Term transactions:
Trades with a fixed maturity date.

Third-party lending:
A system whereby an institution lends directly to a borrower and retains decision-making power, while all administration (settlement, collateral, monitoring and so on) is handled by a third party, such as a global custodian.

Total Balance:
The total value of assets on loan, in USD millions.

Total Daily Return:
The total daily return from both Securities Lending and Reinvestment.

Total Return to Lendable (TRTL):
The revenue from securities lending and reinvestment activity, scaled by the lendable assets, in Basis Points.

Tri Party:
The provision of collateral management services, including marking to market, repricing and delivery, by a third party. Also known as escrow.

Tri Party Repo:
Repo used for funding/investment purposes in which the trading counterparts deliver bonds and cash to an independent custodian bank or central securities depository (the "Tri Party Custodian"). The Tri Party Custodian is responsible for ensuring the maintenance of adequate collateral value, both at the outset of a trade and over its term. It also marks the collateral to market daily and makes margin calls on either counterpart, is required. Tri Party repo reduces the operational and systems barriers to participating in the repo markets.

Utilisation:
The total value of assets on loan over the total value of holdings, expressed as a percentage.

Value at Risk (VaR):
A technique used to estimate the probability of portfolio losses based on the statistical analysis of historical price trends and volatilities.

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