Slow convergence

Philippe Metoudi | AlfaSec Advisors

For more than two decades, Philippe Metoudi has observed the development of markets in the Asia Pacific region from close quarters. *Radar* asked him to sum up the progress he has seen in post-trade operations.

"In 1992, I went to Mumbai to visit a sub-custodian," recalls Philippe Metoudi, now managing partner, AlfaSec Advisors, in Hong Kong. "Someone took me to a gigantic room full of physical certificates. It was shocking; floor to ceiling. He told me that the trade failure rate was 95 percent. I remember asking as a joke if he could show me the

5 percent that settled on time. He said, 'No, I don't know where they are."

From those dismal days, the principal markets in Asia Pacific have made spectacular advances. "Overall, they are in pretty good shape. In the last 10 to 15 years they've made huge progress," says Metoudi. The key markets in the region are close to international standards and in some cases have turned previously perceived drawbacks into advantages. In some markets, for example, accounts had to be held at investor level rather than in omnibus structures. "During the crisis, a lot of investors were asking for their holdings to be in their name and these markets were able to convert problems into competitive advantages," he says.

Markets have also grown in breadth. "When I started my career, there was virtually no securities lending in Asia. Now everybody has it and overall it works fairly well," says Metoudi. He stresses, however, that Asia is far from homogeneous. "Most of the transactions in each market are domestic," he says. "If you talk to Hong Kong investors, the majority of their investments will be in their local market and the same applies elsewhere in the region."

Bilateral links

The impetus for closer operational links among Asia Pacific markets has therefore come mainly from CSDs and exchanges. "They are hoping that by linking to other markets, they will experience an increase in efficiency as well as new revenue opportunities," says Metoudi. There is, however, insufficient volume at the moment to support an expansion in bilateral links. For the moment, he suggests, "We are still looking west and deciding what could be applied in Asia. Believe it or not, there are discussions about having a possible TARGET2-Securities Asia, but that is not something that is going to happen tomorrow given the lack of a common currency." In addition, says Metoudi, part of the ICSDs' strategy is to offer these markets through their hub and spoke structure.

Metoudi does, however, see one new development as a potential game-changer: Shanghai-Hong Kong Stock Connect, popularly known as Shanghai Connect. Launched in late November, this new operational link allows foreigners to access China's mainland 'A' shares through brokers on the Hong Kong exchange (HKEx) and investors on the mainland to buy Hong Kong shares through their Shanghai brokers. Shares bought through Shanghai Connect are held in custody in their respective markets.

The scheme is subject to quotas, both daily and total, which to date have not been exceeded. Purchases through the link are capped at 13 billion yuan a day and 300 billion yuan in total for mainland stocks and 10.5 billion yuan and 250 billion yuan respectively for Hong Kong Stocks.

"In the financial markets in Asia I think you're going to have pre- and post-Shanghai Connect," Metoudi says. "My colleagues at AlfaSec, Roger Harrold and Giles Elliot, have done a lot of work with customers looking to prepare for Shanghai Connect. I think many observers are underestimating its potential impact." He suggests that while initial volumes have been good, it will become an issue of business retention. "If you don't have that capability, you will lose customers," he says.

He does not, however, expect Shanghai Connect to kickstart similar initiatives between other market centres in the region. "Shanghai Connect is an obvious link," he says. "First, Hong Kong and Shanghai sit under the 'one country, two systems' umbrella. Secondly, there is obviously a political will to make this happen." No doubt, he suggests, there are specific investors who would welcome further market linkages for collateral management purposes, but, he adds, "Most of the fund managers we speak to in the region are not that engaged with the idea. Intra-Asian trade volumes are, after all, still quite low." •