

# Automating fixed income in Asia

*Why do some firms automate processing of Asian equities but not fixed income?*

**W**hile the equities world in Asia has benefited from a sustained, widespread industry drive toward automation and straight-through processing (STP) of trades, fixed income has largely remained very manual. Until recently this was acceptable because the Asian bond universe was relatively small, and only affected niche players in a significant way.

The market has changed, however, since the 2008 global financial crisis. First, the region has experienced rapid growth in government and corporate bond issuance. According to a September 2011 report in Asia Bonds Online, the local-currency universe has tripled in size over the past decade, from \$5.4 trillion in 2001 to \$18.1 trillion at the end of 2011. This reflects a widespread desire to improve the local capital markets and broaden financing options amidst an environment of economic growth. It is notable that most Asian markets have reduced their reliance upon foreign-currency bonds whilst growing their local bond markets.

Second, investors from other regions have developed an appetite for Asian debt, although intra-regional investment flows remain low. Liquidity is therefore improving, particularly in the government space. Easy monetary policies in the United States and Europe, designed to keep interest rates as low as possible, have driven investors of all types to eschew bank deposits for higher yields. Emerging-market debt has been a major beneficiary.

Moreover, the healthy macroeconomic fundamentals of most Asian countries make this region attractive to global investors for the long term. However, as both supply and demand increase, there has not been a commensurate improvement in operational efficiency.

Cornelia Dagdag, Omgeo's executive director for sales and solutions delivery, explains what's happening now.

## **Nellie, which instruments in Asian fixed income are most easily automated?**

*Cornelia Dagdag:* Omgeo has dedicated our efforts to post-trade efficiency, or those functions that exist between execution and settlement, across a range of fixed-income instruments, including



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sovereign and corporate bonds and a number of money-market instruments. Even the processing of sukuk (Islamic) bonds can be automated.

Recent growth in dim-sum bonds created a need from within our community to automate processing of these new instruments. To address this, we released a code of practice aimed at reducing manual intervention.

By leveraging an automated environment, the vast majority of Asian bonds can be executed, matched and settled electronically. In addition, Asia-based investment managers and brokers can also process extra-regional fixed income instruments over the same platform.

## **What parts of the post-trade experience are easiest to automate? What parts are harder?**

*Dagdag:* Primarily, breaks in fixed income automation occur when a firm has not invested sufficiently in their operational infrastructure or when it is dealing with counterparties that don't see automation as a priority. In Asia, we find that the latter occurs most commonly in the local broker community. However, we are beginning to see dialogue between these brokers and their buy-side clients around how they can increase efficiency and reduce risk in this area.

The industry is also becoming increasingly focused on the risks associated with settlement failure. In a May 2012 Omgeo study, we estimated that the value of fixed-income trades at risk of failure (on 35 global exchanges) could be as high as \$308 billion.

Our clients, both international and regional, are aiming for complete STP

in fixed income. This includes achieving earlier or even real-time confirmation of trade details between counterparties, thereby reducing the possibility of trade failure due to unmatched details and enabling markets to accelerate the trade lifecycle, while increasing transparency into the trade process. Certainly, this can be done if the right solutions are deployed: a fully automated environment for fixed income trades is achievable.

In addition, many large international investment managers want to migrate to a single global model that can be leveraged across all time zones under a "follow-the-sun" approach. Effectively, this can only be delivered through automation.

## **Is this just a question for COOs or does it involve traders, portfolio managers and senior management?**

*Dagdag:* Primarily automation is being driven by the operations and compliance functions in both buy- and sell-side firms. But the benefits are becoming increasingly well understood at multiple levels within our client community.

We recently held a forum in Asia that brought companies together to look at the benefits and challenges to fixed-income automation. Delegates acknowledged that the optimal processing model for fixed-income instruments involves reducing operational risk and creating scale via end-to-end automation. This understanding does extend to senior management and, in many cases, even the front office. Since the 2008 financial crisis, it has become accepted that the adoption of sound operational practices reduces the potential for reputational risk, and demonstrates stability to investors. ■

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