DERIVATIVES HOUSE OF THE YEAR, ASIA EX-JAPAN

Barclays Capital

Barclays Capital has emerged from being a European debt specialist a decade ago into a global investment banking force able to deliver clients a full range of services from research through to flow trading and complex solutions. It does this across interest rates, currencies, credit, equities and commodities, as well as on both the asset and liability sides of balance sheets. Its growth trajectory has remained on course, despite the global financial crisis of 2007 and 2008. Indeed, the bank's purchase of the north American business activities of Lehman Brothers in 2008 gave it access to large fund flows in the US, as well as an enlarged fixed-income business and a credible equities franchise.

The UK bank has hired hundreds of bankers to build out its cash equities platform in Asia and Europe. This effort has already been completed in Japan and will continue in the rest of Asia until the end of next year, driven by Sigurbjorn Thorkelsson, who joined from Nomura in April to run Asia Pacific equities. It has already given Barclays Capital another important client relationship tool that is also boosting derivatives volumes. "We are now a full-service investment bank, which enables us to showcase our risk management capabilities, including advising companies at how they look at acquisition risk on a holistic basis," says Patrick Kwan, co-head of global financial and risk solutions for Asia Pacific at Barclays Capital in Hong Kong.

This effort extends past M&A. Barclays Capital's enterprise risk management group, set up in July 2009, highlights this approach. This team provides clients with advisory services not just from the traditional aspect of risk management or hedging of market risks, but also utilises quantitative analytics to provide a risk-return perspective on strategic topics such as business growth, acquisitions, capital structure, financing alternatives and liquidity management. "The idea is to offer clients a one-stop shop to understand and diagnose their risk profile on an enterprise-wide basis, and connects them with all the capabilities and solutions provided by Barcap," says Kwan.

Taipei-based Judy Tsai, head of the overseas investment department for Shin Kong Life, whose department manages $16 billion of assets, says Barclays Capital has ascended to the top of the insurer's internal ranking out of the 20 counterparties it has traded with this year. Barclays Capital's ability to underwrite collateralised mortgage obligations (CMO) issued by agencies Freddie Mac, Fannie Mae and Ginnie Mae in the US was a key differentiator. Tsai says the bulk of Shin Kong's investment is in the z-tranches, which start receiving interest and principal payments only after the other tranches in the CMO have been fully paid, but are compensated by the highest yield. So underwriters need to warehouse or place the other tranches with investors before being able to fulfill Shin Kong's demand. "There are some counterparties with whom we placed orders through but, because they could not sell the prior tranches, they had to call off the entire deal," Tsai adds. "Barclays' balance sheet is big enough to enable their traders to hold these positions and wait for the right timing to sell off these prior tranches. It reflects on the bank's strong origination capability," says Tsai, echoing a similar view held by other market participants about the bank's stronger US-related capabilities.

While Barclays Capital lags behind some banks in terms of its local footprint in Asia, the UK dealer has bolstered its onshore presence in Greater China, India and Korea, as well as Australia and Japan. And its efforts to harmonise internal systems, adopt a common view on counterparty credit risks and to work with its treasury unit to agree relatively aggressive funding levels, has enabled Barclays Capital to emerge as a credible competitor to traditional global derivatives stalwarts with a major presence in the region.

For example, a commodities client in mainland China says Barclays Capital has stepped in to provide commodity derivatives support after several major counterparties became less comfortable offering services in China following a number of disputes. In another part of Asia, a local airline says it now conducts the majority of its derivatives trades, valued in the tens of millions of US dollars at a time, with Barclays Capital. "They make a great effort in updating [us on] what is happening in the market, are very responsive to our needs and, when they say they are the biggest commodities trader in the market, I believe them because they execute the trades very well," says the airline's head of treasury. "Other banks have to wait for a long time before they hit the level I want."

Moreover, the London-based bank is also achieving a higher overall level of business per client compared with previous years. That is partly due to its expansion outside of its traditional fixed-income competence, but also reflects its integrated approach to its business in Asia. This integrated thinking has won praise from private bankers, helping Barclays Capital to win *Asia Risk*'s wealth management house of the year (see page 44), as well as with institutional clients. "It is really in the DNA of our culture to promote cross-asset business," says Kevin Burke, head of distribution for Asia Pacific

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Patrick Kwan and Kevin Burke, Barclays Capital

Photographer: Edward Yu

at Barclays Capital in Singapore. "And, frankly, it is the best way to cover the client wallet." Burke says Barclays Capital has made a concerted effort to trade more products with the same clients, adding that in 2006, 32% of accounts traded five or more products with the bank. Now, 56% of accounts are trading five or more products.

Part of this stems from the bank's efforts to focus on its premier clients, which include many sovereign wealth funds in the region, and core hedge funds. "For those two client groups combined, over the last five years we have seen revenue growth at a compound annual rate of 45%," says Burke.

Barclays Capital has also used technology, via its Barx platform, to capture a much longer tail of clients, which helps with flows. The dealer has added emerging markets non-deliverable instruments, for example in renminbi, won and Indian rupee, along with algorithmic trading capabilities to this platform. "We believe we have dramatically increased the breadth of our client franchise over the past few years, particularly during the crisis when competitors were in a period of looking inwards and they weren't really investing or continuing to invest in their franchise," Burke adds.

Singapore-based Ivan Ritossa, deputy head of global fixed income, currencies and commodities, and head of trading for Asia Pacific, who sits on Barclays Capital's executive committee, says the most satisfying achievement during the past 12 months is the way the different facets of Barclays Capital's strategy in Asia have held together in the wake of "extraordinary market moves and market volatility". One of the most dramatic events took place in May as it emerged that peripheral eurozone economies, notably Greece, were overburdened by excessive debt they would struggle to repay. The revelation of sovereign debt problems in the eurozone also caused the euro to tumble 16% against the US dollar between March 18 and June 8, resulting in acute problems for market participants. Equities also fell. For example, the Hang Seng Index lost 14% falling from 22,157 points on April 15 to 18,986 points on May 25 – it has subsequently reversed these declines.

"Between our institutional and corporate client-facing people and our structuring teams, we have done a very good job of staying close to our clients, listening to their needs and working with them to provide derivatives-based solutions in what have been challenging markets," says Ritossa. "We have consistently invested in technology and have increased the focus on our flow business, and so have been able to recycle our risk. By doing so, we never reached a point where our risk books were saturated."

Its funding levels have also helped bolster trading flow. One example was the bank's ability to use its derivatives technology and its extended client franchise to offer long-dated, KRW/USD cross-currency swaps (CCS) for a Korean corporate and a large US insurer this year. By acting as an intermediary between two clients with opposing financial needs – the corporate had an existing US dollar liability that needed to be swapped back in Korean won; and the insurer needed long-dated won-denominated assets – Barclays Capital succeeded in marrying their liability and asset needs by structuring two CCS trades that resulted in a natural offset and cancelled out the exposure of the two sides. The deal size, in the range of $50–100 million, overcame problems with liquidity in the Korean CCS market, where bid/offer spreads become very wide for transactions longer than 10 years and achieved the yield enhancement required by the insurance client. "If you had to offer that structure without the benefit of having a hedge – or linking up the opposite position of the Korean corporate and the insurer-investor – it will become expensive," says Amit Agarwal, managing director for rates structuring for Asia Pacific at Barclays Capital in Hong Kong.

On the liability side of the trade, Agarwal's team ended up with a long-dated won cross-currency structure where Barclays Capital pays US dollar interest (Libor) and the corporate client pays Barclays Capital won fixed interest rates. Due to the principal exchanges in the CCS, Barclays Capital ended up being long-dollar and short-won cash. As the investor was looking for a long-dated won asset, whose limited supply means there tends to be limited yield pick-up alternatives for investors, Barclays Capital created a long-dated asset that could offer yield enhancement for the investor through a CCS. The aim was to create that asset without being constrained by the illiquidity in a typical CCS of that tenor. To match up the liability with the asset, Barclays then issued a non-deliverable forward (NDF) structured note, similar to the tenor of the original CCS-linked trade done with the corporate. The investor pays won cash to buy the note and receives won fixed rate through the note. Since this is non-deliverable, all cash flow payouts to and from the investor are converted into dollars at the prevailing exchange rate at conversion time.

To provide the investor with the benefit of yield pick-up on the structure using Barclays Capital's structured note funding levels, among other hedges, the bank did a separate cross-currency swap, swapping the won cash proceeds from the issuing of the NDF note into dollars, then deposited the dollars with the bank's money-market desk. The investor trade hence created a second CCS exposure, which was opposite of the liability trade, where the bank ended up long won cash (from the note) and short dollars, resulting from the bank lending the dollar cash to its money-market desk. Barclays Capital then pays won interest (to the investor through the note) but receives dollar, at Libor plus a spread, from the bank's money-market desk for the dollar funding. "The positions created by the original liability trade for the corporate and investor trade are opposite and offsetting and achieve a win-win situation for the investor and us – it gets us out of an illiquid risk and the investor gets a long-dated asset with good yield pick-up. The trade was possible only by linking two sides of opposite risks created and needed by the market," Agarwal says.

Barclays Capital's currency derivatives platform, meanwhile, has drawn praise from clients and competitors alike – particularly the bank's technology platform. James Iorio, head of forex sales for Asia in Tokyo, echoes his colleagues, saying the challenges of the financial crisis did not result in a loss of focus: "We have been able to do what few of our competitors could: grow a client-centric business through financial strength, product innovation and global delivery."

Iorio says the bank operates a currency platform across asset, liability and advisory approaches. He adds that while the past year saw a shift away from the asset side, this trend may now be coming to an end as appetite from Singapore and Hong Kong private banks for forex-linked structured products has been growing. One transactional highlight from the asset side is a new index – the Commodity Producers Currency Index (CPCI) – designed to capture the impact of rising commodity prices on resource related currencies. "Playing the commodity story using currencies allows investors to enjoy positive roll yield, making it an attractive way to express a bullish view on the performance of commodity-rich economies over the medium to long term," says Giovanni Armanti, director in the forex structuring group in Singapore.

On the liability side, meanwhile, the bank has invested in operational capacity to better serve globally integrated clients. The opening of a Shanghai branch has given the bank a foothold in the onshore markets, which it hopes to leverage with Chinese and global clients. Elsewhere, the dealer has set up a cross-region execution platform to deliver hedging solutions for Asian corporates' pan-Pacific operations out of Latin America. "Barclays Capital is good in both hedging and investments," says Jerry Tsai, manager for forex structuring at Fubon Bank in Taiwan. "Their pricing is good, they have a very fast turnaround time and they offer a very good mark-to-market service."

In the commodity derivatives area, Barclays Capital continues to hold an edge over many of its competitors through its ability to provide access to some 1,200 different types of commodities worldwide. "Our commodities business model is a diversified model, aimed at providing our clients with access to a wide variety of commodities, through a range of solutions and across geographies," says Peter Rozenauers, a director and head of Asia commodity sales at Barclays Capital in Singapore.

That range of solutions spans all the way from simple flow derivatives through to highly structured products, with feedback from clients consistent in their appreciation for the bank's ability to provide access to the right commodities, via the right solutions and at the right price. "We deal with Barclays Capital on a regular basis and they're always capable of providing us with access to the risks we are looking for, structured in ways that match our exact requirements," says one senior portfolio manager at a large fund management firm in Asia Pacific.

While investors have traditionally sought exposure to commodities by investing in long-only standard beta transactions, in recent years so-called enhanced beta and alpha strategies have become popular, designed to minimise the risk of negative carry putting a dampener on index returns. That has reduced the appeal of passive, beta-tracking indexes, many of which roll futures in the most liquid front-month contracts, where negative roll yield is typically most pronounced. Instead, it has resulted in a strong focus on enhanced beta indexes that seek to mitigate the problem of negative roll yield by investing in futures further down the curve, or market-neutral alpha strategies that balance long and short indexes to provide investors with pure curve exposure.

Barclays Capital is also active in providing liquidity and solutions across a full-range of credit products globally. The bank offers a range of flow and structured/correlation products. It is also actively working with its clients to expand the universe of credit default swap names in Asia as well as seeking to develop onshore, local currency credit derivatives markets.

The UK dealer's equity derivatives business, meanwhile. demonstrated its ability to offer innovative transaction and ongoing clever positioning for the future. Deals included a breakthrough into the Malaysian Islamic structured products market via a landmark deal with Bank Islam, as well the bank's ability to sell volatility as a decorrelated asset class to Asian retail investors. In parallel to this, the bank has invested heavily in systems, including the Comet platform. Alongside Comet, this January the bank rolled out its Bmarkets platform for the exchange-listed and traded retail structured investment business in Hong Kong for warrants and callable bull/bear contracts (CBBCs), which has enabled it to ramp up issuance volumes in this area and also provide secondary market trading and pricing – as part of the firm's aim to grow its listed business.

Ramping up the bank's flow business, through initiatives such as Bmarkets, is expected to have a knock-on effect for flow structured products – as the flow derivatives enable the dealer to recycle its risk. "We have put in place a successful client tiering, which has improved our client focus and servicing," says Nicholas Cohen-Addad, global head of electronic trading for equities and funds structured markets in Hong Kong at Barclays Capital.

It is a business strategy that seems to be working.

Ivan Ritossa,
Barclays Capital