

FOCUS ON

INDUSTRY INNOVATION: THE BLACKLIGHT PLATFORM



It shines light where there is darkness, makes visible that which is opaque and provides authenticity to the phony. A blacklight can provide a stamp of approval for everything from bank notes to antiques, show you the perfect detailed imperfections of fine art, and highlight the psychedelic, mind-bending messaging embedded in a 1960s poster.

It is under this transparent-seeking name that a new software has launched to help illuminate the notoriously complex prime broker-hedge fund dynamic.

Designed and hosted by financial analytics firm S3 Partners, the BLACKLIGHT technology enables asset managers to benchmark financing costs and fully optimise relations with their prime brokers through a range of analytics and customised, high-touch services.

It has been dubbed 'the world's first counterparty intel analytics (CIA) platform' by the New York-based firm, which believes the new tool is already redefining how managers and brokers can help one another conduct business more efficiently.

“ [BLACKLIGHT] GIVES CLIENTS THE VISIBILITY THEY NEED TO UNDERSTAND THE MARKETPLACE. MORE IMPORTANTLY IT HELPS THEM UNIFY COST, UNDERSTAND WHERE RESOURCES ARE BEING SPENT AND WHICH RELATIONSHIPS ARE ACTUALLY CREATING ALPHA FOR THEM

” ROBERT SLOAN, S3 PARTNERS

The relationship between a prime broker and hedge fund is changing. With banks adopting regulations, an increasing concern among managers is how to manage the intersection of big data, fintech and regulation. The demands for enhanced transparency, strong custody and greater operational accountability in the brokerage space are louder than ever.

As the latest instalment of Basel III comes into force, capital, liquidity and leverage requirements for banks are tougher than ever. With common equity tier 1 capital levels rising from 2% to 7%, the balance sheet



pressure on prime brokers to raise their return on assets (ROA) and capital difficulties facing hedge funds means a relationship once defined by wallet share is now centred on how much capital, funding and balance sheet is used.

A report released earlier this year by investment bank JP Morgan, titled *Leveraging the Leverage Ratio*, reiterated the need for better relations with service providers.

“Managers should understand in detail the holistic value of their relationship with the prime broker’s organisation, considering all elements of wallet allocation,” the paper read.

“Managers should develop a transparent dialogue with their prime brokers in order to understand the value that their business represents and the metrics prime brokers use to evaluate this business.”

This desire for dialogue and openness has led to the emergence of an array of online tools. BLACKLIGHT’S software-as-a-service platform and its high touch service desk offers a comprehensive set of cost mapping, market monitoring and reporting techniques to the increasingly diligent asset manager.

Officially launched in May this year, BLACKLIGHT



streamlines and aggregates all relevant securities finance, margin and SWAP data from asset managers and benchmarks the cost of financing specific securities, services and risk exposure with prime brokers and custodians.

By comparing a client's short and long positions, the software can compare them against market composite rates and produce data to show what the true financing rate in the market is.

"It gives clients the visibility they need to understand the marketplace. More importantly it helps them unify cost, understand where resources are being spent and which relationships are actually creating alpha for them," says Robert Sloan, S3 Partners' managing partner.

The platform also pinpoints any variances in the market at a given time and allows managers to see where potential savings on the short/long side can be made. With a built-in price improvement function that lets managers send revised financing rates straight to their prime brokers, BLACKLIGHT believes it can greatly improve transparency.

"It is a great fiduciary tool and allows price improvement but at the same time keeps the relationship intact with the counterparties," says Manny Santayana, global

head of business development at S3 Partners.

Furthermore, the in-house built technology gives managers the opportunity to analyse the breakdown of their wallet across all prime broker relationships and see clearly how costs fluctuate across different firms.

This facility to examine all of one's portfolio, as well as locating information on any specific security, helps provide a much stronger overview of fund activity. "You can get a complete understanding of what is driving cost/resource use on a fund level or on a provider level basis and you also have the ability to chart all that information historically," says S3 Partners' Rocco Nisivoccia.

With Basel III honing in on balance sheet stability, BLACKLIGHT'S innovative software enables users to see a coherent picture of balance sheet usage – which positions and providers are balance-sheet intensive and what is driving return for providers.

Sloan says: "Each large investment bank is going to have limited access to balance sheet, much more limited than they had before – so efficiency is on the top of their priority list and BLACKLIGHT actually helps the provider become more efficient and the client to see how they can be a better client while monitoring and actioning their entire enterprise cost, service and risk equation."

Collating data from prime brokerage firms and other institutions, BLACKLIGHT also offers users the chance to see a heatmap of real-time market activity and where potential covering and shorting is taking place.

It can provide insight beneficial to all facets of an asset management firm, as Sloan remarks: "It is a tool to unify all the jobs that exist for an asset manager. This is a way of unifying the financing part of the firm and making sure that the portfolio manager, trader, CFO and COO all get on the same page."

By streamlining all data and creating checks and balances to improve risk management and compliance, BLACKLIGHT can help deal with the mounting challenges faced by Basel III and is, according to Sloan, "the Volcker Rule for borrowed money."

There are 43 asset managers – with combined assets of more than \$300bn – currently using the software and just as the ultraviolet blacklight makes evident the invisible, S3 Partners' BLACKLIGHT platform can bring greater transparency to the ever-demanding investment industry.

“

IT IS A TOOL TO UNIFY ALL THE JOBS THAT EXIST FOR AN ASSET MANAGER. THIS IS A WAY OF UNIFYING THE FINANCING PART OF THE FIRM AND MAKING SURE THE PORTFOLIO MANAGER, TRADER, CFO AND COO ALL GET ON THE SAME PAGE

”

MANNY SANTAYANA, S3 PARTNERS

BLACKLIGHT gives the manager a tool to customise reporting and to measure the relative value of cost, risk, service and regulation in the Basel III world.

As Sloan concludes: "You cannot be a hedge fund manager today without having a handle on the costs, risks and information that comes out of the marketplace." ■