

SECURITIES LENDING IN FOCUS

In this piece, we explore the purpose and mechanics of securities lending programmes within ETFs.

- 1 WHAT IS SECURITIES LENDING?
- 2 WHAT ARE THE RISKS ASSOCIATED WITH SECURITIES LENDING?
- 3 WHAT IS THE GLOBAL X APPROACH TO SECURITIES LENDING?
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KEY TAKEAWAYS



Securities lending is a well-established practice of loaning the holdings of a fund in order to generate additional income, with the objective of providing increased returns to a fund and reducing investors' net costs. Global X ETFs takes a prudent approach to securities lending where the securities are always over-collateralised to minimise counterparty risks. Global X has robust policies in place for securities lending designed to ensure the best possible risk and reward profile for Investors' portfolios.



1 WHAT IS SECURITIES LENDING?

Maximising returns in physical portfolios

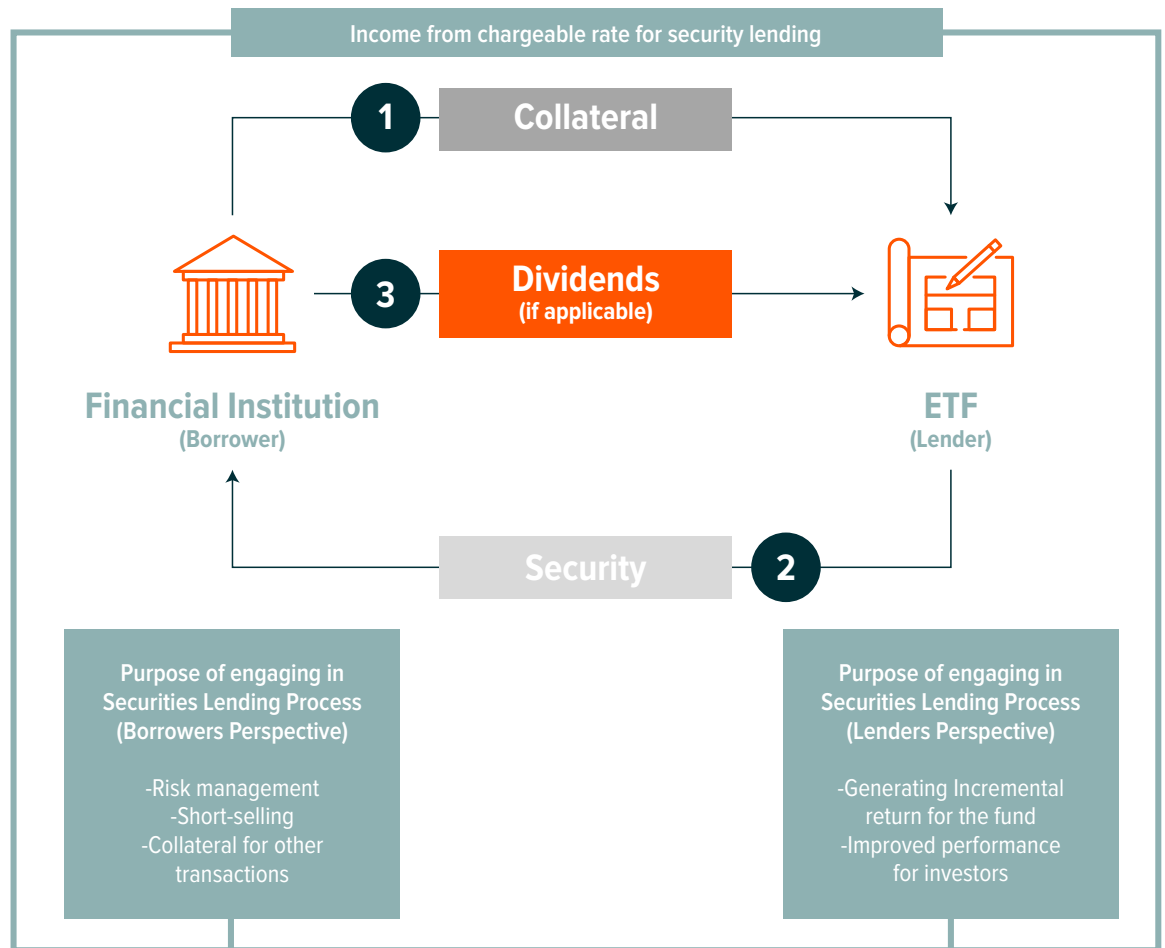
- Securities lending in simple terms is a process whereby the holder of a security temporarily loans the security to a borrower in return for a pledged collateral and a fee. Securities lending is deployed broadly by many long-term holders of securities in the investment industry as a means to gain additional income and enhance fund performance. The securities lent out are typically the stocks or bonds being held by the fund as part of its portfolio.
- The collateral required from the borrower is pre agreed and is held as a security against the risk of the borrower defaulting while they have the security on loan. Typically, the collateral the borrower is required to pledge will exceed the value of the securities that are lent out to help ensure the fund is protected if the borrower defaults.
- The borrower can have varying motivations for requesting to borrow the security, this may range from hedging activities, meeting settlement obligations or taking short positions. The fee generated for the fund lending the security is a function of the supply and demand of the security being loaned.
- While the security is on loan income such as interest and dividend payments flow back to the lender of the security and if the lender wishes to exercise voting rights on the security, they have the discretion to recall the securities. At the end of the loan term the security is returned to the lender and collateral flows back to the borrower.



Figure 1: Process of Securities Lending

SECURITIES LENDING VISUALISED

Source: Global X ETFs, as of Jun 30, 2022



Dashed lines indicate the final stage of Securities Lending transaction where the Borrower returns the security to the Fund. In turn, collateral is released back to the Borrower. This successfully completes the process.



2 WHAT ARE THE RISKS ASSOCIATED WITH SECURITIES LENDING?

- As with any source of investment return there is risk involved. However, securities lending programmes are designed to mitigate the associated risks and protect the lender. The key sources of risk in securities lending are the that the borrower of the security defaults.
- Brown Brothers Harriman & Co. (BBH) is the global sub-custodian and the securities lending agent for Global X ETFs. BBH is responsible for managing the overall securities lending process for Global X ETFs and help safekeeping of Global X ETFs' financial instruments and cash. BBH's credit rating, which has remained unchanged over the years, was recently confirmed January 2021 by Fitch with a Long Term Debt rating of A+, Short Term Debt rating of F1 and a viability rating of A+.
- Default risks exist if a counterparty fails to meet its contractual obligation and deliver the securities back to the ETF. Global X and BBH are very selective in approving the right counterparties during the securities lending process. BBH approved borrowers represent the largest and most creditworthy in the industry, with the overwhelming majority designated Systemically Important Financial Institutions (SIFIs).



- Global X seeks/aims to mitigate its counterparty risks through BBH's indemnification for counterparty default, including borrower's failure to return loaned securities (i.e., not limited to insolvency events only). BBH will apply collateral held to purchase replacement securities and unpaid distributions, and if the cost of replacement securities and unpaid distributions exceeds the value of the collateral held, BBH is responsible for the shortfall.
- Market risks arising from daily price movements of the loaned securities and collaterals will also impact the value of the lending portfolio. Under our current indemnified lending program for borrower default, it assumes the market risk arising from the price volatility of lent securities (that must be replaced) following a borrower default. As such, our lending program is subject to continual assessment including a daily value at risk (VaR) calculation and daily liquidity monitoring of loaned securities.



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WHAT IS THE GLOBAL X APPROACH TO SECURITIES LENDING?

- Global X ETFs take a prudent approach to securities lending. While UCITS directives allow for a fund to lend up to 100% of its securities, Global X has capped its lending at 50%. The lending programme for Global X ETFs passes back 87% of revenue to the fund.
- Borrower approval is subject to multiple levels of review and limited to highly credit worthy financial institutions. Borrowers are carefully selected and before receiving securities on loan the borrowers must pledge collateral. Global X transactions in securities lending are always over collateralised.
- Financial health of counterparties is evaluated on a daily basis incorporating a number of exogenous factors to stay ahead of rating agency downgrades and on an interim basis between the release of periodic financial statements. These factors include publicly available market information, including financial statement review, CDS pricing, transaction flows and shifts in demand patterns. Borrower credit line utilization is controlled on a pre-trade basis with a buffer for market value fluctuations
- BBH, our securities lending agent, offers indemnification for counterparty default, including borrower's failure to return loaned securities. Indemnification is not limited or capped. BBH's credit rating, which has remained unchanged over the years, was recently confirmed January 2021 by Fitch with a Long Term Debt rating of A+, Short Term Debt rating of F1 and a viability rating of a+.

POLICY OVERVIEW

Source: Global X ETFs, as of Jun 30, 2022

Securities Lending Agent	Brown Brothers Harriman (BBH)
Eligible collateral	Government Issues Debt issues by France, Germany, Netherlands, Sweden, Switzerland, the U.K. and the U.S
Minimum Collateral Levels	105%
Proportion of Fund NAV subject to securities lending	0-50%
Maximum proportion of the fund NAV of the fund to be used for securities lending	50%
Percentage of securities lending revenue to be received by the fund	87%
Percentage of securities lending revenue retained by securities lending agent	13% (including direct and indirect operational costs and fees of the securities lending)
Securities lending report publication frequency	Monthly



4 FREQUENTLY ASKED QUESTIONS

Q) DOES GLOBAL X HAVE A SECURITIES LENDING PROGRAMME AND COLLATERAL MANAGEMENT POLICY?

Yes, Global X has a formal securities lending programme and collateral management policy approved by the Board of Trustees for UCITS ETFs.

Q) WHAT IS THE DUE-DILIGENCE PROCESS FOR DETERMINING THE LIST OF AUTHORISED COUNTERPARTIES FOR SECURITIES LENDING?

Both the Securities Lending Agent (BBH) and Global X Management Team perform a continual analysis of counterparty risk for the securities lending programme by monitoring credit default swaps, credit ratings and other public or proprietary metrics of risk.

Q) HOW DOES GLOBAL X DECIDE WHICH SECURITIES ARE PERMITTED TO BE LOANED OUT?

Selected Global X ETFs are eligible to participate in securities lending across UCITS and US-domiciled product suite. The Independent Board of Trustees must first approve a Fund for securities lending. The underlying securities of each approved Fund are all eligible for this programme, but there is a monitoring process in place to lend securities which have greater revenue opportunities. All current Global X UCITS ETFs participate in securities lending. For the Irish-domiciled ETFs, regulatory requirements dictate that no more than 100% of an individual Fund's securities can be out on loan. Global X has approved an internal policy that lowers the limit to 50%.

Q) WHAT ARE THE REQUIREMENTS FOR COLLATERAL MANAGEMENT?

Global X UCITS ETFs only accept highly liquid government debt as collateral, reducing liquidity concerns. Our Agent Lender (BBH) provides an indemnity on the collateral market value.

Q) WHAT RULE DOES GLOBAL X FOLLOW FOR SECURITIES LENDING PROFIT SHARING WITH INVESTORS?

The Prospectus Supplements for Global X UCITS ETFs specify that the Funds will retain 87% of securities lending revenue.

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For more insight, view our Global X Monthly Securities Lending Report on www.globalxetfs.eu

The value of an investment in ETFs may go down as well as up and past performance is not a reliable indicator of future performance.

Trading in ETFs may not be suitable for all types of investors as they carry a high degree of risk. You may lose all of your initial investment. Only speculate with money you can afford to lose. Changes in exchange rates may also cause your investment to go up or down in value. Tax treatment depends on the individual circumstances of each client and may be subject to change in the future. Please ensure that you fully understand the risks involved. If in any doubt, please seek independent financial advice. Investors should refer to the section entitled "Risk Factors" in the relevant prospectus for further details of these and other risks associated with an investment in the securities offered by the Issuer.