Not so SWIFT to address weak points

REUTERS, *Belgium*

MORE than a dozen current and former board directors and senior managers of SWIFT, the bank messaging system that helps transmit billions of dollars around the world every day, have told Reuters that the organisation for years suspected there were weaknesses in the way smaller banks used its messaging terminals – but did not address such vulnerabilities.

The sources said that until February, when hackers tried to steal nearly $1 billion by breaking into the messaging system at Bangladesh's central bank, SWIFT had not regarded the security of customer terminals as a priority. Top executives either did not receive information from member banks about specific attempts to hack the messaging network, or failed to spot those attempts themselves, the managers said.

In SWIFT's annual reports and strategy plans from the past 17 years Reuters could find only one reference to SWIFT helping its users to secure their systems. That reference – to helping "our community to strengthen their own infrastructure" – was in the 2015 annual report published in June this year, months after the Bangladesh heist, in which the fraudsters ended up making off with $81 million.

"The board took their eye off the ball," said Leonard Schrank, who was chief executive of SWIFT from 1992 to 2007.

Schrank said he was broadly aware that users' terminals were a weak link in SWIFT's overall security, but paid too little attention to it. "So I am partially responsible," he said.

The messaging business failed to act in part because the risks were not properly appreciated, the former directors and managers said.

SWIFT did not comprehensively track security incidents or monitor the extent of sloppy security practices among users. It saw smaller banks as a potential – but not immediate – threat to the security of the network, according to the former managers and directors.

SWIFT never acted, former board member Arthur Cousins said, because the organisation believed bank regulators – rather than SWIFT – were responsible for ensuring smaller banks' security procedures were robust enough to repel hackers.

A spokeswoman for SWIFT, a cooperative owned by banks, defended the organisation. "SWIFT and its Board have prioritised security, continually monitoring the landscape and responding by adapting the specific security focuses as threats have evolved. Today's security threats are not the same threats the industry faced five or ten years ago – or even a year ago – and like any other responsible organisation we adapt as the threat changes."

SWIFT was, and still is, dominated by large Western banks, including Citibank, JP Morgan, Deutsche Bank and BNP Paribas, that built the network decades ago. That contributed to the lack of concern over security, said the former directors, because the larger banks tend to have sufficient defences to prevent criminals from hacking into their SWIFT systems. But since the 1990s, many smaller banks in emerging markets have joined SWIFT, and some may have weaker computer security.

Gottfried Leibbrandt, CEO since 2012, said it was only with the benefit of "hindsight" that one could see that SWIFT needed to put more focus on security at customer terminals. "Hindsight is always a wonderful thing," he said. "Sometimes it takes a crisis to change things."

In the Bangladesh heist, hackers broke into a computer interface called Alliance Access, a piece of software sold by SWIFT for accessing its central network. It is still unclear exactly how the thieves gained entry. Bank Bangladesh has alleged that a botched upgrade of its system left vulnerabilities in it. SWIFT has rejected any responsibility for the way Bangladesh Bank upgraded its systems.

Whatever specific weakness the thieves in the Bangladesh case exploited, former SWIFT directors and managers said the system became more vulnerable as it got bigger.

Alessandro Lanteri, a former executive with Italian bank Unicredit who served on SWIFT's board between 1995 and 2000, said security challenges increased when smaller banks in emerging markets joined the SWIFT network. "The difficulty is always to keep the security system very effective when you deal with little banks and emerging countries," he said. "There, it is very difficult to be sure that all the procedures of security are managed in the correct way."

Bigger western banks considered SWIFT more cost effective and secure than alternative means of communication, Cousins said.

But despite the rise in the number of smaller institutions as members, the big banks continued to dominate SWIFT. The organisation's revenues, which hit 710 million euros last year, are driven by a concentrated number of large western correspondent banks like Citigroup and HSBC, former SWIFT staff said.

Traditionally, 90 percent of messaging revenue comes from banks in just 25 countries – almost all developed markets – data in the decade to 2011, the last year for which SWIFT published a breakdown, shows.

Some people working at the coalface spotted evidence of deteriorating security well before this year's Bangladesh case.

Two years ago, Martin Ullman, a Prague-based SWIFT consultant, was browsing a LinkedIn forum for SWIFT users when he saw a posting from a recently-appointed technician at the Central Bank of Solomon Islands (CBSI). The technician needed to install an upgrade to the bank's SWIFT messaging system but didn't know how. He wanted advice.

Ullman emailed the man and told him that raising such issues in a public forum could endanger security and advised him to seek expert help. The technician said the bank couldn't afford it, and said he finally managed to install the system himself. CBSI declined to comment. Reuters was unable to contact the technician to confirm the incident.

Yet security was vital: Six former directors of SWIFT said any breach of the broader system could put the bedrock of SWIFT – the willingness of banks to accept messages at face value – at risk.

Hugh Cumberland, a former SWIFT executive who now advises banks on payments technologies, said he first saw security risks in 1993. He told Reuters that, when he was working as a technology contractor with BZW, an arm of Barclays, in London. Cumberland arrived for work one day to be met by policemen carrying Heckler & Koch submachine guns. Two staff members had been arrested for attempting to use their access to a SWIFT terminal to send 10 million pounds of "unnamed client money" to accounts controlled by them. Cumberland did not know the outcome of the case. Both SWIFT and Barclays declined to comment.

Another incident occurred in 1995, when officials at Dubai Islamic Bank (DIB) began sending fraudulent payment instructions to Citibank, telling it to pay money from DIB's account at the US bank into the account of a fraudster, according to a lawsuit DIB filed against Citibank in New York in 1999. More than $150 million was allegedly stolen by DIB executives in collaboration with Foutanga Dit Babani Sissoko, a West African businessman previously jailed for trying to bribe US customs officials. Reuters could not contact Sissoko.

A lawyer involved in the case confirmed the messages were sent via SWIFT. The court dismissed the claim of negligence against Citibank. The banks declined to comment on the case.

More recently, thieves exploiting SWIFT systems stole $250,000 from Bangladesh's Sonali bank in 2013 and more than $12 million from Ecuador's Banco del Austro in 2015. Later in 2015, Vietnam's Tien Phong Bank foiled an attempt to steal money via SWIFT. SWIFT officials said the banks involved in these three cases did not immediately inform it of the incidents, though the banks did confirm them later.

The senior management at SWIFT appears to have been unaware of the events. Leibbrandt told Reuters in May that, before the Bangladesh heist in February, he had not been told of any successful or unsuccessful attempt to steal money using SWIFT.

Asked why SWIFT had not logged the incidents described above, a spokeswoman said: "SWIFT has always maintained an uncompromising focus on security as evidenced by our track record."

Some former SWIFT executives and directors said the failure to spot the security risks around user terminals reflects weaknesses in SWIFT's board. Schrank, the chief executive from 1992 to 2007, said some directors lacked the experience needed to help steer such a big and important enterprise.

"Generally the SWIFT board, with very few exceptions, are back-office payments people, middle to senior management," he said.

Fritz Klein, a former Credit Suisse banker who served on SWIFT's board from 1998 to 2002, said an even greater concern was the length of tenure of some members, which he said did not encourage fresh thinking. At any time, a third of members had been there for "very long, perhaps too long," he said.

A spokeswoman for SWIFT said: "SWIFT's large and diverse group of Board members have decades of experience in operations, management, IT, risk assessment, and various other disciplines. SWIFT's Board composition includes long-standing members with a deep understanding of how SWIFT works, as well as newer members who contribute with a fresh outside view."

AirAsia India outlines plans to expand fleet, network

REUTERS, *Bengaluru*

Budget airline AirAsia India said on Wednesday that it planned to gradually expand its fleet and network in India as it seeks to boost its small market share in the fast expanding domestic market.

The airline, a tie-up between Malaysian carrier AirAsia Bhd and India's Tata Sons conglomerate, said it planned to add a seventh A320 jet to its fleet and bring the south Indian city of Hyderabad into its network of destinations by September.

Speaking at a press conference on Wednesday, AirAsia India's Chief Executive Amar Abrol said the airline is looking to expand further and that it would be investing significant sums of money in the future.

REUTERS/FILE

AirAsia aircraft sit on the tarmac at Singapore's Changi Airport.

China police crack down on $30b in underground banking

REUTERS

Chinese police have busted underground banks that handled 200 billion yuan ($30.2 billion) in illegal money transfers this year, the Ministry of Public Security (MPS) said on Wednesday.

Police said they arrested 450 suspects involved in 158 cases of underground banking and money laundering, according to a notice posted on the MPS official website.

Beijing has been fighting illegal cross-border outflows in an attempt to slow capital flight as its yuan currency weakens to near six-year lows.

A special task force, jointly launched by the MPS, the central bank, and the foreign exchange regulator, uncovered illicit banking services in 192 locations this year, the notice said.

On Wednesday, China state broadcaster CCTV separately reported that police in the southern city of Shenzhen recently busted an underground bank that handled 30 billion yuan in transactions over a six-year period. Police arrested 26 major suspects in four different cities, the report said. The underground bank was disguised as a trade company.

Political risk? Banking crisis? Investors buy euro zone debt anyway

REUTERS, *London*

UNRELENTING demand for fixed income has pushed yields, in Europe at least, to a point where investors no longer distinguish one country's bonds from another's -- potentially storing up trouble for when focus returns to the economic drivers behind borrowing costs.

Individual countries' credit ratings, political risks and fiscal and economic performance have been pushed aside as a global hunt for yield has gathered pace since Britain voted in favour of leaving the European Union in a June referendum. The result darkened Europe's growth outlook and triggered a fresh wave of monetary easing from central banks.

Highlighting the impact on yields, lower-rated Spanish 10-year government bonds have joined their higher-rated peers in France, Belgium and Finland with a yield at record lows below 1 percent.

That pushed the yield gap over top-rated German bonds to just over 100 bps - levels that in the past have not been sustained for long periods.

In Italy, which has a lower credit rating than Germany and France, 10-year yields are just above 1 percent and at levels some fund mangers believe do not reflect banking sector problems or political uncertainty linked to a looming referendum.

"There's barely any discrimination among sovereigns anymore," said Frederik Ducrozet, senior economist for Europe at Pictet Wealth Management. "It's a potential recipe for disaster if and when those bonds are repriced."

The European Central Bank's 1.74 trillion euro asset-purchase scheme provides a powerful buffer to regional bonds and made them less sensitive to country-specific dynamics.

But investors are not completely shielded from a change in market sentiment or a trigger for a broad sell-off that could see the bloc's weakest members bear the brunt of selling.

Analysts point to last year's unexpected bond rout, triggered by a pick-up in inflation as an example. While German Bund yields rose about 100 bps between April and June last year, Spanish and Italian yields climbed over 120 bps each.

A sell-off in Portuguese bonds on Tuesday after ratings agency DBRS said pressures were building on Portugal's country's creditworthiness was also a reminder of just how quickly yields can rise when focus returns to domestic issues.

Potential triggers for a reassessment of the bond market could come from economic data or outside Europe if talk of another U.S. interest rate hike gains ground, analysts said.

"In a scenario of a large generalised pull-back in government bonds yields, the most perceived risk are likely to be the most vulnerable. This is what we saw in March-June last year," said Antoine Bouvet, rates strategist at Mizuho International.

"In the case of the periphery, there is currently enough risks to those countries to expect that spreads will widen in a generalised sell-off."

A Federal Reserve official said on Tuesday there could be as many as two rate hikes before the new year, and another said a move could come as soon as next month.

As this graphic shows, tmsnrt.rs/2aUpm0I, since Britain voted in June to quit the European Union, yields across Europe have fallen sharply to close proximity to each other.

With more than $13 trillion of government and corporate debt yields globally in negative territory, investors have been pushed into seeking higher returns in longer-dated debt, lower-rated peripheral bonds and emerging market debt.

That help explains why yields on Spanish and Italian bonds are lower than those on benchmark U.S. 10-year Treasuries, which stand at 1.58 percent.

For Oksana Aronov of JPM Income Opportunity Fund, the backdrop of negative yields is one reason why bonds have become less sensitive to "fundamentals" - the economic and political dynamics that usually effect the pricing of a bond.

"Bonds have long served as the anchor in a conservative portfolio, a "safe-haven" asset with an income component designed to produce a consistent return stream," she said in a note.

Given the rise in negative-yielding debt, "bonds increasingly cease to trade based on fundamentals, such as yield, and trade instead on what someone else might be willing to pay for them in the future," Aronov added.

With little difference in yield between European issuers, it is even more important to do a "fundamental analysis" because taking on extra risk is not compensated for with a higher yield, said David Zahn, head of European fixed income at Franklin Templeton Fixed Income Group.

"That may be fine for the next 6-12 months but someday fundamentals may come back and you could see an aggressive re-pricing."

REUTERS

Euro coins are seen in front of displayed flag and map of European Union.