

The rise of the CCP - What it means for CSDs

Hugh Simpson
Bourse Consult

AMEDA Conference, November 2014

Pittsburgh Declaration (2009)

- *Improving over-the-counter derivatives markets:* All standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest. OTC derivative contracts should be reported to trade repositories. Non-centrally cleared contracts should be subject to higher capital requirements. We ask the FSB and its relevant members to assess regularly implementation and whether it is sufficient to improve transparency in the derivatives markets, mitigate systemic risk, and protect against market abuse.

Use of CCPs

Instrument	Traded on exchange	Traded over the counter (OTC)
Derivatives	Always	Pittsburgh Declaration
Securities	Often	Not common

Reasons for using a CCP

- Counterparty credit risk reduction

Guarantee fund + pre-positioning stock and cash

Replaced by

Dynamic margin model + collateral

Reasons for using a CCP

- Counterparty credit risk reduction
- Operational risk reduction

Netting reduces transaction volumes and volatility

Reasons for using a CCP

- Counterparty credit risk reduction
- Operational risk reduction
- Supporting market structure:

Pre-trade anonymity
needs

Post-trade anonymity

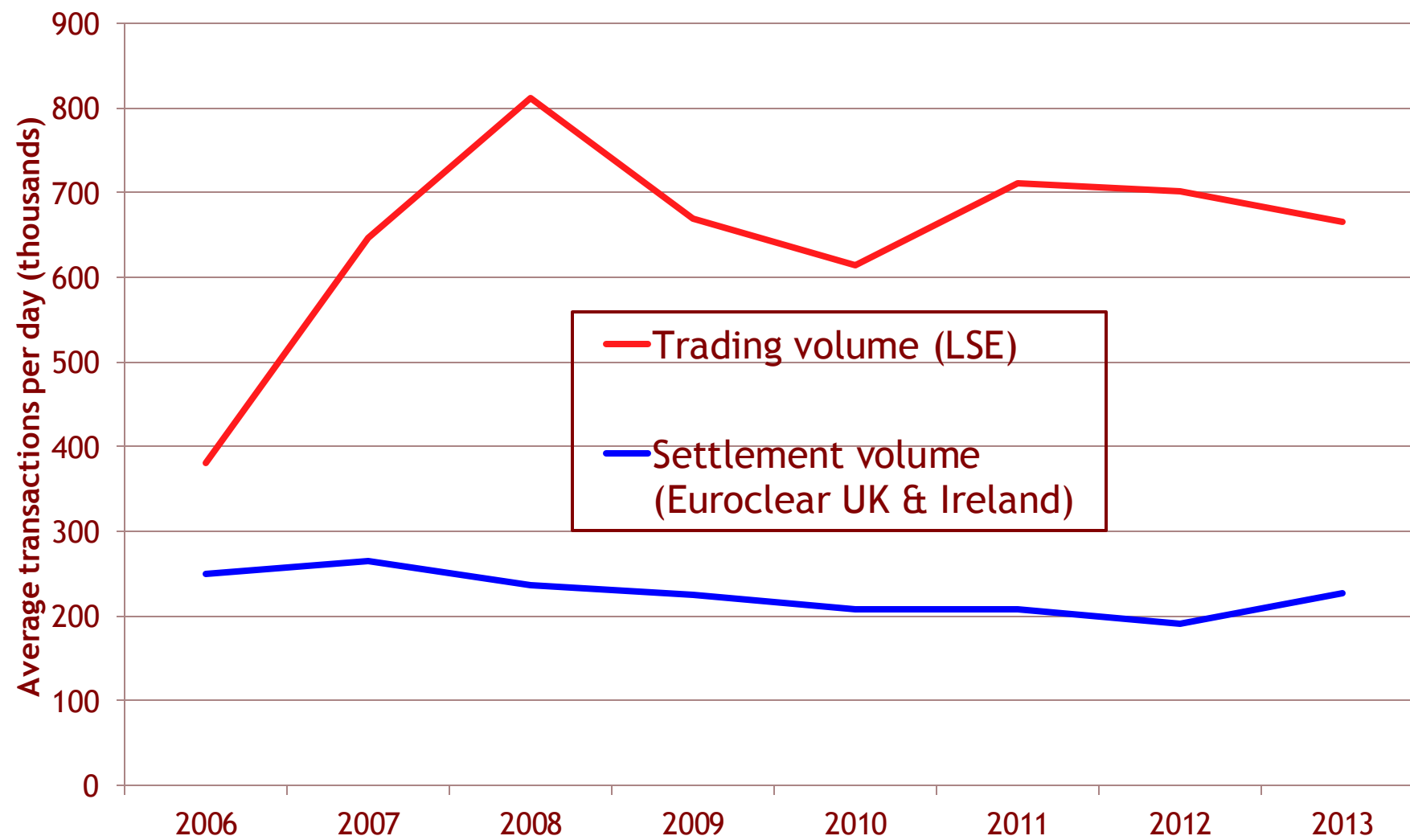
What it means for CSDs

- Reduction of settlement volumes
- One very large settlement participant

BUT

- Less volatility in settlement volumes
- More open to international participants
- Larger market in total
- Less responsibility for risk management

UK trading and settlement volumes



The impact of netting

Type of transaction	Netted?
Client to broker	<input type="checkbox"/>
Broker to broker - on exchange	<input type="checkbox"/>
Broker to broker - OTC	<input type="checkbox"/>
Securities lending	?
Repos	?
Custodian to custodian	<input type="checkbox"/>

Options for CSDs

1. Build the CCP

Can a CSD be a CCP?

Similarities:

- Both are post-trade infrastructures
- Need ability to process high transaction volumes efficiently
- Similar client base

Differences

- Risk profiles: CSD avoids risk, CCP accepts risk
- CCP may handle derivatives, CSD not

Conclusion: may be better as sisters

Options for CSDs

1. Build the CCP
2. Provide services to the CCP

CSD services for a CCP

- Transaction processing vs risk management
- Corporate action management
- Securities lending

Options for CSDs

1. Build the CCP
2. Provide services to the CCP
3. Restructure sources of income

CSD sources of income

Source of income	Affected by CCP netting?
Transaction settlement fees	Yes
Membership fees	No
Custody charge	No
Value-added services	Possibly increased

Should CSDs be afraid of the CCP?

- Introduction of a CCP is a major change for the CSD
- But it also creates opportunities for CSDs
- And it can create a larger more dynamic market

Thank you

hs@bourse-consult.com