

Live and let fly

Panellists discuss progress in Eurex Clearing's Lending CCP, and what flow is expected in 2014



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What has been happening with the Eurex Lending CCP in the last 12 months?

Markus Büttner: A lot has happened behind the scenes here. After we helped our first clients to go live with the service at the beginning of 2013, discussions with other banks evolved from mandates to evaluation of their business case, to detailed specification work and connection to the service. In short, the first question asked is no longer 'should we'; it has become, 'how can we'.

For existing clients, we have performed the adaptations for the new services offered, ie, introduction of fixed income instruments and ESES (French, Dutch and Belgian) equities, as well as Eurex Repo's securities lending market as a new electronic marketplace.

Frank Gast: We at Eurex Repo have focused on providing our securities lending market in time, which we technically integrated earlier in 2013. Again, with the support of DekaBank and Maple, we are proud to announce that the first trades have successfully been executed in our securities lending market and passed the Lending CCP in production.

Thomas Wißbach: Eurex Clearing has developed the service further over the past year: new markets, new assets classes, new asset servicing capabilities and new flow providers have all been introduced to the Lending CCP service to offer an even more efficient and cost effective service available to our members.

Walter Kraushaar: We were always supportive of the Eurex Clearing's Lending CCP product, as we firmly believe that this market segment will become extremely important in the light of the required implementation of the new Basel III rules. It will become essential for most of the market participants to have access to central counterparty platforms in general. We expect a substantial shift of liquidity through the Eurex platform and we wanted to be among the first participants, because we had a unique chance to provide input into the product and make it compatible with our existing platforms from the very first day.

Michael Cyrus: As an early adopter, we appreciate the enhancements to the service, and also the opportunity to use Eurex Repo's securities lending market to access it. While we would love to see volumes increasing at a faster pace we are also getting signals from our counterparties that they are looking into the Lending CCP business opportunity with great interest. For DekaBank, using Eurex Repo's securities lending market as an additional platform was a logical conclusion after using Eurex Repo services for many years. Eurex Repo was already integrated and our internal lending CCP processes established. We expect that via Eurex Repo's securities lending market, more existing trading counterparts will join the Lending CCP environment.

Capital efficiency is perceived to be one of the major pros in the Lending CCP. Is it even possible to calculate this advantage pre-trade and how it relates to the cost?

Cyrus: The regulatory landscape is still fluid, rather than being a solid block, so you can measure and calculate with precision. Balance sheet, liquidity and capital are being re-priced in the current regulatory overhaul. Now, these three factors happen to be the primary resources of any financing business and, as a consequence, will have a huge impact on the business of collateral trading and collateral transformation. Each bank is currently in the process of addressing this regulatory pricing conundrum, and it is advisable to invest into a strategic setting that will ensure you will not be caught out by the re-pricing of collateral transformation.

Collateral optimisation in the future will not just be an internal exercise, it will be about platform optimisation as well, and it is here, where the Lending CCP will certainly play its part.

Wißbach: Although there are many complex factors that are required to be taken into consideration to even begin this analysis, and many of these factors are different for each participant, Eurex Clearing has been able to clearly break down the significantly reduced capital costs that are available to our clearing members if they were to use the Lending CCP for a portion of their existing securities lending transactions. The Lending CCP certainly contributes to a more efficient and cost effective way to manage regulatory capital and associated costs.

Kraushaar: CCPs are one tool for managing capital, balance sheet, liquidity and collateral more efficiently. However, there are many more regulatory changes to come such as the liquidity coverage ratio (LCR), which requires a much broader view on the general business strategy of a bank. For many current businesses, it is not attractive or even possible for them to be in line with all the new regulatory changes starting in 2015. To only look at CPP platforms is not enough to manage the liquidity of a bank in a professional way.

Büttner: For all of our clients, this is a question to be answered, but how easy it is to find the answer is very different. First of all, you would have to take all advantages that the CCP brings to a trade into consideration, and weigh it up with an equal bilateral trade.

Pros such as exposure netting, operational support during the lifecycle, and settlement might be equally hard to number exactly, but are an important part of the equation. Some institutions we are consulting in this matter have made good progress in allocating cost and benefits to the respective business units, while others are in the middle of implementing such processes.

Gast: In addition to the advantages of the Lending CCP, EurexRepo's securities lending market brings additional benefits. For example, all our existing repo customers now have the opportunity to join the securities lending market without changes in the technical infrastructure, thereby realising synergies between our different funding and financing markets, ie, addition sources for loan and collateral with positive balance sheet impacts in a regulatory friendly environment.

Eurex Clearing's Lending CCP is also supporting the agency lending model. What's your view on the adoption of this in the market?

Gast: Our securities lending market has recently been enhanced with an agency model and will further attract new target groups such as funds, insurance companies and asset managers, which so far have not been able to participate in our interbank repo markets.

Cyrus: Agency lending offers a couple of characteristics that will be interesting from a collateral trading perspective in the new regulatory world. Market participants who are looking into the most efficient set up with regard to the costs of credit line utilisation, leverage ratio or capital utilisation—just to name a few—will certainly have to look into agency lending as a further instrument to achieve their goals.

Consequently, we will have a closer look in 2014 as to whether the CCP is something we would want to offer to our beneficial owners in the short term. But of course, this will certainly also depend on the benefits the beneficial owners see for themselves.

Kraushaar: The agency lending business in general is another important product to optimise the trading of collateral from a regulatory point of view. Many of the existing agent lenders are already working on a solution to combine a CCP platform with their existing product. Beneficial owners are also heavily affected by the new regulations, and they will definitely have to adopt the connection to a CCP to their lending platforms in order to keep their balances with borrowers stable. There are already projects up and running to also integrate triparty agents into this process, to offer an even more competitive product to the market.

Büttner: We are driving both topics at the same time for some of our customers, with the CCP and agency lending being seen as an answer to requirements arising from the current regulations. The specific lender license offered to beneficial owners definitely lowers the entry barrier for them to join the CCP, allowing them to participate without having to post margin. The discussions about the future of indemnification and whether a lending CCP would have the potential to replace this guarantee is certainly key, which is why we bring agent lenders and their benefi-

cial owners together within our mandates to find answers to this paramount issue.

Wißbach: By introducing this innovative structure that allows agent lenders' customers to remain in their current principal role and still continue to use the expertise and infrastructure of an agent lender, the Lending CCP creates the ability for all securities lending participants to broaden their range of trading counterparts, thus simplifying the counterparty credit structure, minimising credit lines and above all, mitigating risk. This is a main driver that makes central clearing attractive for this market.

What do you expect for 2014 to happen with lending CCPs?

Kraushaar: We will clearly see a big shift of business from a bilateral basis into CCPs. This has already begun, as all the banks have to prepare their business for a new regulatory world, which will begin in 2015. The speed, however, will be dependent on the products a CCP can offer, ie, what kind of securities can be traded through a CCP, how competitive are the margin requirements, etc. CCPs now have the chance to usurp rivals by becoming more responsive to market participants needs and regulatory requirements. I am convinced that the Eurex Clearing Lending CCP product has a good chance to gain significant market share quickly.

Gast: Having done a lot of ground work in 2013, we feel confident in expanding our business with the integration to Eurex Clearing's Lending CCP service. Our existing client base already has demands for the connectivity options and models offered. This also means a more harmonised cross-market and cross-product service offering going forward.

Wißbach: We have seen a firm shift in opinion; large-scale borrowers and lenders now need to realise the opportunities that are available. We shall see this trend continue this year, when there will be increased levels of activity at the banks that are signing up to the service. These early adopters will benefit. Big advantages will accrue to the agent lenders from the borrowers that get involved now.



Cyrus: We certainly believe that the commitment we and other institutions have put into the service as first movers has been important to overcome the 'chicken and egg' situation any new service in our industry faces. However, CCPs are a large part of the future world. The benefits in terms of netting, credit exposure and capital are for real and will become more pronounced as the regulatory steamboat picks up pace. We expect serious business.

Büttner: As a strategic advisor we already have new assignments in 2014 to neutrally evaluate with our customers the most efficient way to connect to the service. With new flow providers at the horizon, it is not only a technical question as to which one to choose, but more a process on the business side. Within this year, Comyno will furthermore launch a bundled advisory and software package to significantly shorten the onboarding time, as we firmly believe that a wave of new memberships is approaching.

The nice thing about being a firm with the unique competence in this field is that we are actively contacted and asked for help by the potential participants. I am looking forward to the rest of this year, and I'm convinced that we have put Comyno into a position to significantly contribute to the success of our customers in this market. SLT

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