



CCPS: YOU'LL NEVER WALK ALONE?

Richard Metcalfe, Head of Regulatory Affairs, World Federation of Exchanges

Webinar

Monday, 02 August 2021, 15:00 BST

A Word From Today's Chairman



Professor Michael Mainelli

Executive Chairman

Z/Yen Group



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GIBRALTAR STOCK EXCHANGE

Today's Agenda



- 15:00 – 15:05 Chairman's Introduction
- 15:05 – 15:25 Keynote Presentation – Richard Metcalfe
- 15:25 – 15:45 Question & Answer

Today's Speaker



Richard Metcalfe

Head of Regulatory Affairs
World Federation of Exchanges

Poll 1



Is the world a better place for being more collateralised than it was 10 years ago?

- a) Yes
- b) No
- c) Not sure



YOU'LL NEVER WALK ALONE?
~
C.C.P.S AND THE FINANCIAL SYSTEM

RICHARD METCALFE, HEAD OF REGULATORY AFFAIRS, W.F.E.

FS Club webinar

August 2021

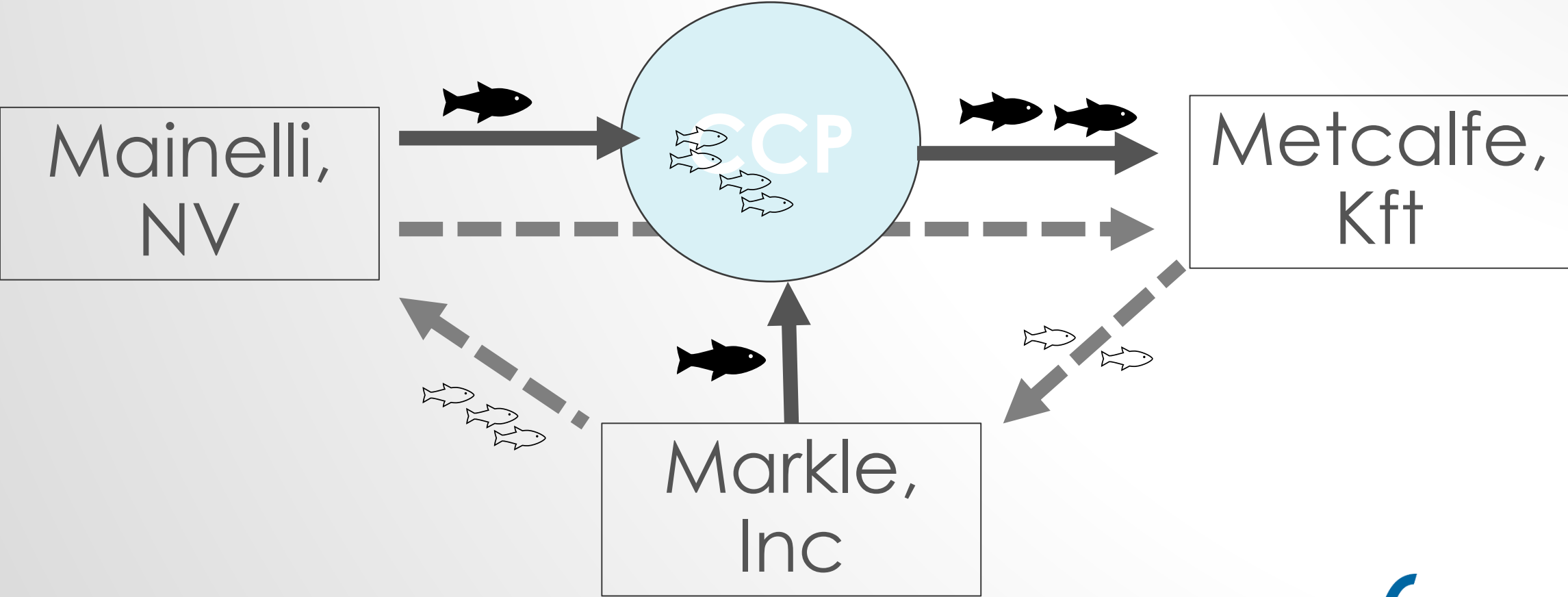
WHAT A CCP IS... AND IS *NOT*

- A *clearing* service – **distinct from settlement**
 - Reduce counterparty exposures, even for trades with no final settlement;
 - You still need the CCP, even if there are no new trades
- A commitment mechanism -- not a credit portfolio
 - continuity of position; defined user group
 - risk co-ordination with users; clear, equitable rules
- A mutual *in extremis* (which keeps users focused)
- Polluter pays
 - CCPs back their ops with capital; 'skin' is for signalling alignment – not loss absorption; users have to back *their* risks

BACKGROUND INFORMATION

- WFE members run 55 CCPs
 - Variation margin – a daily back and forth; \$30-80bn (FSB Holistic Review 2020)
 - *plus* ~\$1 trillion of over-collateralisation (initial margin); *plus* ~\$100m default fund
 - VM covers MtM on ~\$100tr *notional* in ETDs + ~\$300tr cleared OTC
 - OTC markets added \$1tr of collateral since the GFC (Cunliffe, June 2020)
- Comparisons:
 - CLS settles ~\$50bn a day net (eliminating 99% of the gross)
 - www.newyorkfed.org/medialibrary...14-CLS-2015-Kos
 - WFE exchanges: netting out anything up to 99% of exposures

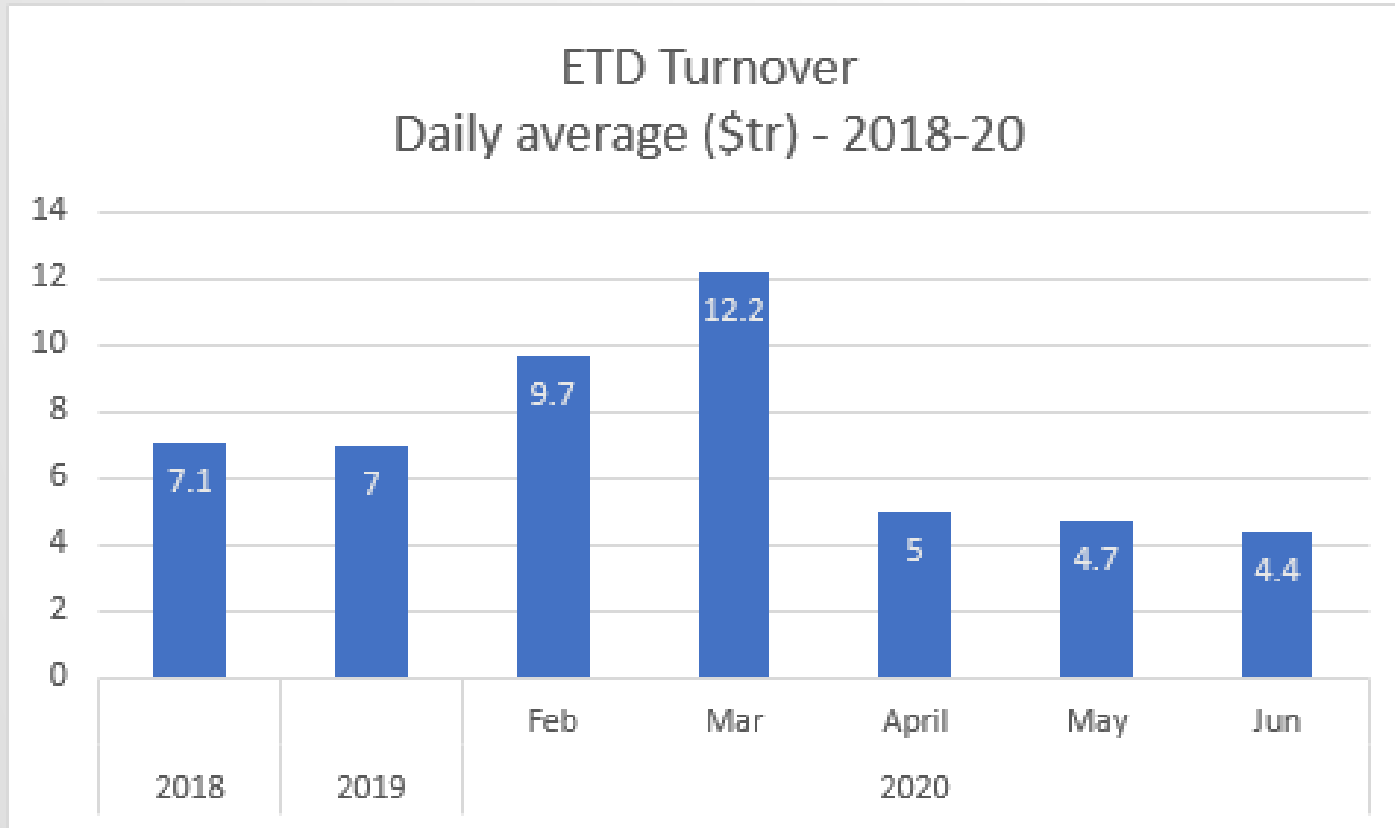
NETWORK NETTING EFFECTS



THE DOG THAT DIDN'T BARK

- Counterparty fears 2020: conspicuous by their absence
 - “Prompt margining avoids a situation in which the perceived stress on one major player leads to a panic because of **uncertainty** about who else might be exposed, how great the exposure is and whether it is adequately protected by margin.” (Cunliffe, Nov 2020)
- Even some buy-side estimate future liquidity requirements. Why not all firms?
 - A common issue “...banks are having to apply [VaR-model] multipliers because of market volatility rather than shortcomings in their models”. (ISDA, April 2020)
- “Daily demands due to additional IM requirements were notably smaller [than] VM calls.” (FSB, Nov 2020)
- Procyclicality is a system-wide issue – not CCP-specific

DYNAMIC DERIVATIVES SYSTEM



Volumes surged in spring 2020

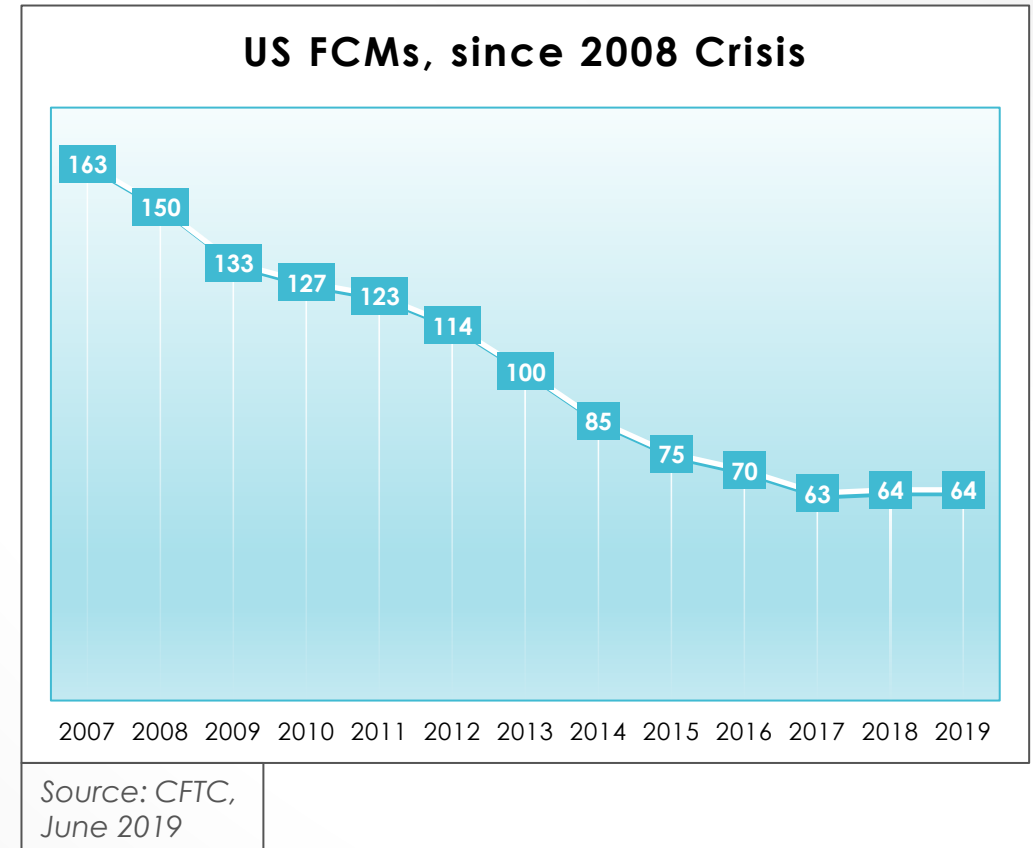
Increased activity (and volatility) led to higher margin requirements

(OTC turnover figures not yet available)

Source: BIS

'DON'T GO CHASING WATERFALLS'

- CCPs' role is to *help* the system – not backstop it
 - Non-default losses are manageable; but default by >2 large users could be challenging
 - Lehman's portfolio managed with \$\$ to spare; but FCM market is now more concentrated requiring more vigilance than ever from CCPs banking supervisors
 - 3-4 = 50% of US market.
 - Promising to compensate users after CCP failure makes an unlikely event more likely



CCP RESOLUTION



Beware the fallacy of ex-parrot revival.

But avoiding resolution is in everyone's interests.

FOOD FOR THOUGHT

- **CCPs' role in systemic safety 4 Dec 2019**
 - It took a collapsing banking and credit system in 2008 for the wider world to see what some already knew: that there is a major role for neutral, central entities who can enforce discipline on risk takers and, in the process, reduce systemic risk.
 - CCPs' own resources perform an important but entirely distinct role, backing their own operational continuity and signaling their responsibilities to measure and monitor accurately and impartially the degree of risk being taken in the market.
- **Guidance on non-default losses 11 Jun 2020**
- **Response to FSB: treatment of CCP equity in resolution 29 Jul 2020**
- **Response to CPMI-IOSCO: Default Auctions 12 Aug 2019**
- **Margin models: a systemic approach 12 Jan 2021**





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- Tue, 3 Aug (10:00-10:45) Augmenting The Augmentors - How The Great Western Metaverse Will Be Built
- Thu, 5 Aug (11:00-11:45) A World Of Individual Opportunity: The Vision Of Egalitarian Capitalism
- Mon, 9 Aug (10:00-10:45) The Real Deal: Is Your Leadership Team Truly Capable?

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