Central clearing in fixed income markets

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The dynamic CCP landscape

• Regulation is a key driver of changes in the organisation and behaviour of CCPs and the markets they serve.

• Recent SEC rules on clearing of US Treasury securities have opened the discussion on the structure and functioning of fixed income cash and repo markets across the globe.
The European fixed income market

- The European fixed income market is characterised by a larger degree of fragmentation and is more reliant on primary dealers (especially for government bonds) compared to the US market.
- The role of NBFIs in liquidity provision is seemingly less important – yet more data on this would be welcome.
- The European repo market is also essentially different from the US repo market, with a sizeable share of trading executed on venues and cleared by CCPs, and a limited triparty segment.
Recent stress events and margin procyclicality

- Margins are procyclical by nature as they increase in periods when volatility is high and risks grow, so that to protect clearing members from the consequences of a future default by other members.
- European regulation includes provisions aiming at mitigating excessive margin procyclicality.
- In addition, global initiatives such as the recent work by BSBS, CMPI and IOSCO aims at increasing transparency of margin requirements as a policy measure to avert destabilising spirals between margin calls and market liquidity.
CCPs acting as market players in the European repo market

• CCPs are central to financial markets in various ways including by an interplay between central clearing and funding (repo) markets, which highlights the importance of European CCP supervision
• This is also relevant to the discussion on granting CCPs access to central bank facilities raised by the CCP industry
• ESMA uses a number of supervisory tools to examine risks relevant to CCPs including CCP stress tests, which examine the resilience of EU and Tier 2 CCPs to a wide range of risks, while also taking a look at the impact of a possible spillover of risks to the wider CCP ecosystem