EUROPEAN CENTRAL BANK

EUROSYSTEM

ECB-PUBLIC

ECB Operations Managers Group

Frankfurt am Main, Wednesday 6 March 2019, 13:00 – 17:00 CET

Summary of the discussion

1. Introductory remarks

U. Bindseil, Director General for Market Operations of the ECB, welcomed the Members of the ECB Operations Managers Group (hereafter "the Group"). He referred to the achievements of the Group and stressed the importance for the ECB to be regularly updated on post-trade developments of a regulatory and technological nature, and further on cyber security and other operational risks. He encouraged further cooperation between the Group and the other market contact groups (MMCG, FXCG, BMCG). Within the ECB, not only the market operations area should benefit from the insights of the group, but also others with responsibilities and/or interest in post-trade issues. U. Bindseil also recalled that the Group's procedures for membership and transparency have been aligned with those of the market contact groups. Finally, he announced that Emily Witt (ECB) will succeed to Michel Stubbe as Chairperson of the Operations Managers Group as from the next meeting onwards.

2. Annual Statistical Report on EU Derivatives Markets

C. Winkler (ESMA) presented the key findings of ESMA's first annual statistical report on EU derivatives markets, based on data collected under the European Markets Infrastructure Regulation. He emphasised the responsibility of ESMA as regulator to make visible use of regulatory data – the annual statistical report is the first of a series of statistical reports published (EU derivatives markets, cost and performance of retail investment products, alternative investment fund markets) or in preparation.

He gave a comprehensive overview of the functioning of derivatives markets for the year 2017. Key aspects are: (i) the size of EU derivatives market at around EUR 660tn, (ii) OTC derivatives still being dominant compared to exchange-traded derivatives, (iii) the rise of contracts for difference (CFDs), and (iv) increasing clearing rates for derivatives subject to clearing obligations, which is a signal for the effectiveness of the clearing obligation.

All in all, C. Winkler confirmed that the data provides a robust market overview, however he highlighted that continuous efforts to further improve the quality of the data are needed both for reporting entities and regulators. Members reflected on the importance of implementing best practices and sharing expertise across jurisdictions, with the UK and the US in particular, to foster improved efficiency on their side.

3. Update on Brexit preparations

S. Rosati (ECB) reviewed implications of Brexit from the perspective of Financial Market Infrastructures, both in the case of a deal and no deal scenario. In view of the significant amounts cleared for euro area clearing members in UK CCPs (58 trillion of OTC derivatives according to trade repository estimates last October 2018), she emphasised the public action undertaken to address the possibility that legal or operational risks may have arisen for EU27 market participants in a cliff edge scenario without sufficient mitigating actions, i.e. the conditional and temporary (one year) recognition of UK CCPs by the European Commission and ESMA in case of no-deal, without prejudice to future EMIR2 implementation. The UK CSD Euroclear UK and Ireland, would similarly be granted temporary recognition for a period of two years in the case of a no-deal scenario to avoid possible negative impacts on the Irish securities markets. From a trade repository perspective however, a no deal Brexit entails porting stock of current transactions recorded at a UK trade repository to a EU27 authorised trade repository.

In terms of impact on actual payments and back-offices access to T2 and T2S, the T2 Guideline already envisages modalities for access by third-country entities. For the cash leg, this can be done via a (duly authorised) EEA branch or subsidiary or indirectly, as a BIC addressable institution via a correspondent bank. So even if there is no need to amend the legal provisions, some UK participants may need to re-route their payments or adjust their entry point to T2. As to the securities account in T2S, its access is ruled by the CSDs themselves.

Members reiterated the significant costs implied by Brexit for their own institutions, included in post-trade and reporting compliance of newly EU27 set-up entities.

4. Introduction of euro-risk free rates: operational implications from a back-office perspective

Two presentations were given with the objective to show the implications of the changes on post-trade activities. P. Quiralte (Cecabank) reviewed the initiatives taken at his Bank to address the concerns over the integrity and reliability of a reference rate in their legal documentation. He explained the wide use of Euribor-linked financial products such as OTC derivatives, debt securities and loans, which impacts a large range of stakeholders.

Y. Santalla (ECB, Secretariat to the working group on euro risk-free rates) gave an update on the work done by the working group on euro risk-free rates highlighting possible implications for all market participants. Members underlined the time criticality to receive final guidance from the working group and from market associations for the implementation of their own legal action plan for contracts based on the old benchmark terminology. They also need time for the set-up of systems and workflows, and to assess risk management and accounting implications. They insisted that the recommendation of a fallback rate for Euribor and the methodology that would be based on (backward-looking versus forward-looking methodology) would have further operational and legal implications.

The Secretary of the working group encouraged market participants to follow working group developments as timely work is in process.

5. Introduction of initial margin requirements for non-centrally cleared derivatives

A. Kraft (Deutsche Bank) briefly recalled the background to the introduction of initial margin (IM) for non-centrally cleared derivatives, from the G20 initiatives in 2009 aiming at reforming the OTC derivatives markets, to EMIR. The exchange of IM introduced by the regulation prevents the build-up of uncollateralised exposures within the system, but triggers major operational implementation challenges in view of its application for Phase 4 and Phase 5 clients in September 2019 and September 2020.

First, from the observation period March-May used to determine the scope of application and the implementation deadline, A. Kraft underlined the very short timeline for the set-up of the underlying legal agreements, including the IM calculation framework. While additional clarifications on the legislation are still required, in particular on the documentation requirement where the counterparties intend to make use of the threshold, operational burden mainly stems from the long process to open accounts with custodians and the corresponding exchange of collateral schedule. Further, and despite the general adoption of the SIMM method published by ISDA, internal models may be applied differently for certain products, and this has operational implications. Overall, A. Kraft noted the fragmentation of collateral processes, the increase in margin movements, as well as the need for improved calculations capabilities. Members highlighted the exclusion of FX-based instruments from IM. Further discussions addressed the segregation requirement for IM collateral in general and the different legal requirements regarding securities versus cash accounts.

6. Robotics Process Automation: current perspectives and challenges

S. Forrest (UBS) started his presentation with an overview of his group’s operations experience with RPA. He explained that operations is the first function of the bank having developed robotics on a large scale and covering a broad work application spectrum, from FX processing to automatically generated interest claims and settlement fails chasing activities.

R. Venugopal (Société Générale) reviewed the main challenges faced with RPA, whereby 30 to 50% of RPA projects tend to fail in the financial industry, in the context of an initial surge in scouting for basic robotics applied on repetitive tasks. This can be attributed to issues related to a strong dependency of built-in systems, the maturity of the technology, and governance. For instance, he noted some challenges encountered by robots in accessing certain applications. There are also challenges to implement automations of conversations or making use of data visible directly from a screen. Members insisted on the governance between IT and RPA teams being distinct and pursuing different objectives. Members explored the possibility to release payments by robots, which is a source of internal challenges. They emphasised that task automation is more a reality than process automation with the prerequisite for saving costs being in the redesign of processes.