



David Holcombe

FX Clearing – Foundations for the Next Generation of FX

By David Holcombe, Product Lead for FX Futures and Clearing, 360T | Deutsche Börse Group

HOW MUCH AND WHO'S ASKING?

Even though right now the bulk of the five plus trillion dollars FX ADV remains OTC executed and underpinned with bilateral credit, the G20 in Pittsburgh 2009 charted a new course for the derivatives market by triggering regulation that has forced pre-trade transparency, competitive execution, trade reporting, and central clearing into this traditionally bilateral market. This journey has not completed, but while the landscape may look at first glance to still be the same as

it ever was, the FX market has already fundamentally changed.

After several years of client focus on ensuring compliance with specific regulatory mandates, the majority of clients we meet now seem to have moved into survival mode - where having now baked-in MiFID compliance costs on top of the previous Dodd Frank, EMIR, Basel III costs before, we are seeing a real shift to actively explore how to use exchange-traded products and central clearing of OTC FX trades, to achieve the right trading result

in a more cost-effective manner. While one Asset Manager recently commented that "it would be nice to get back to a market where managers are seeking alpha, not obsessing on cost savings", that's not an accurate picture of everything that is going on. As Deutsche Börse Group's FX unit we are engaging with real pioneers in the FX industry. Trading, investing, and clearing firms who know how the market is changing and are now making their land grab in the new landscape, by being liquidity provider or taker in new FX

products, and by setting up their client clearing offerings ready to capture rising interest.

BUT WHY ALL THE FOCUS ON CLEARING? WELL, HOW LONG CAN YOU IGNORE THE POTENTIAL FOR 9BP SAVINGS PER MILLION TRADED?

Clearing is a tool that delivers operational benefits including multilateral netting and protection of assets within the Clearing House, but the savings from clearing can be material. We typically see up to 9bp savings, which is \$900 saving per million USD traded. However, the decision of what to clear when, is actually complex and sensitive to many things including client type. While banks have strongest case to clear, we now invite market participants of any type who are seeking to understand the benefits to use a model we have created with Oliver Wyman that allows us to tailor results for any client type that considers the 43 variables which determine what parts of their FX portfolio they should clear and why, and where the use of Futures instead of Forwards or other OTC positions can help optimise their trading outcome.

Clearing banks are starting to grab the opportunity in FX. Beyond self-clearing to exploit the available savings on House business, it looks

inevitable that FX client clearing will echo the battle of single dealer platforms to win hearts and minds of clients during the electronification of the FX market. We are going to see the clearing brands that are first to facilitate clients' OTC and On-Exchange FX Clearing with an accessible and well-priced offering, picking up many OTC participants who are moving from entirely bilateral activity.

BUT WHY NOW? WHAT'S CHANGED?

The timing is right. It has taken a long time for the industry to get here, but with the forthcoming Deutsche Börse Group Eurex OTC FX Clearing service, the ability to use discretionary clearing for more than just OTC NDF is becoming a reality. With this service, participants will be able to clear their OTC FX Forwards, FX Swaps, alongside OTC Spot and also Cross Currency Swaps, alongside their Listed FX activity. From a client perspective, Deutsche Börse Group is the only exchange group with a joined-up FX clearing proposition that comprises both OTC deliverable FX and On-Exchange FX products, plus bilaterally settled or centrally cleared products, with all of this being available through 360T.

While other exchange groups with OTC acquisitions will follow to present on-exchange,

cleared, and bilateral OTC FX in a single platform, the first parts of this are available now in 360T. Clients can already access the exchange orderbook for FX Futures through 360T, with this literally running alongside their bilateral OTC FX activity. From this summer, 360T clients will be accessing the first pool of streaming electronic liquidity of off-exchange FX Futures, using familiar disclosed OTC execution models. Then Client clearing of OTC FX trading activity will complete the suite.

THE NEXT GENERATION OF FX

The next generation of FX is not attempting to move the entire FX market into exchange products. As the Deutsche Börse Group model shows, there are material economic benefits in using Listed FX products in order to amplify the benefits of clearing while minimising margin burden, but the next generation of FX is actually entirely about client choice. With 360T, Clients have a single, reliable platform in which they can exercise their choice of using an OTC or Listed FX product, with the right execution model that is either disclosed or undisclosed, all with the right clearing and settlement model, to achieve the most cost-efficient results for their portfolio, so that they can thrive in the new landscape.