

POST TRADE OPTIMISATION: A NEW ERA IS EMERGING

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The era of large-scale regulatory programmes such as MiFID2, EMIR and Dodd-Frank is starting to cool off. The current regulatory agenda is becoming more focused on specific areas, such as collateral management, settlement discipline and an increased scope on regulatory reporting. It is time to take a more holistic focus on post trade optimisation and define and execute a strategy across all functions.

In the first in our content series on post trade, we introduce the key themes and opportunities in clearing, collateral and liquidity management.

Collateral Management – Time For More Joined-Up Thinking?

Collateral has taken centre stage in recent years, its rise in prominence emerging from a programme of regulatory and industry reforms in response to the global financial crisis. The wider adoption and extended use of collateral to mitigate counterparty risk across a broader range of transactions has created higher demands on access to quality collateral at a global level.

Despite the growing demand for collateral at enterprise level, many firms still take a parochial approach to collateral management, with duplication across multiple business areas and locations. When most firms are seeking to reduce operational risks and costs, achieve capital efficiencies while growing revenues, it begs the question – is this model still fit for purpose to meet current and future business needs?

The thought of embarking on a multi-year, costly transformation programme to rationalise your collateral footprint is a daunting prospect for most firms. However, there are opportunities to deliver real cost and efficiency benefits that can be achieved for relatively modest investment and within reasonable timeframes to meet ROI thresholds. Here, we highlight some of those opportunities:

T2S – adoption of central bank money

T2S, the pan-European securities settlement platform was initially conceived to standardise and harmonise settlement in Europe and lower costs to a level to compete with the US. One of the overlooked benefits was the opening of access to central bank money for buy-side and sell-side firms. This has advantages over liquidity funding in commercial bank money and allows for more efficient use of collateral to significantly reduce funding costs and reduce counterparty risk. For example:

- RWA efficiencies – central bank money attracts a RWA of 0% compared to the 20% attributed to commercial bank money. This reduces the levels of collateral set aside for regulatory capital purposes.
- Lower liquidity funding costs – central bank liquidity has a 0% funding cost (excluding collateral custody fees). The use of central bank money frees up collateral locked in to cover intra-day liquidity exposures and T2S allows for the use of auto-collateralisation to minimise the committed collateral for central bank liquidity.

Consolidation of CCP clearing operations

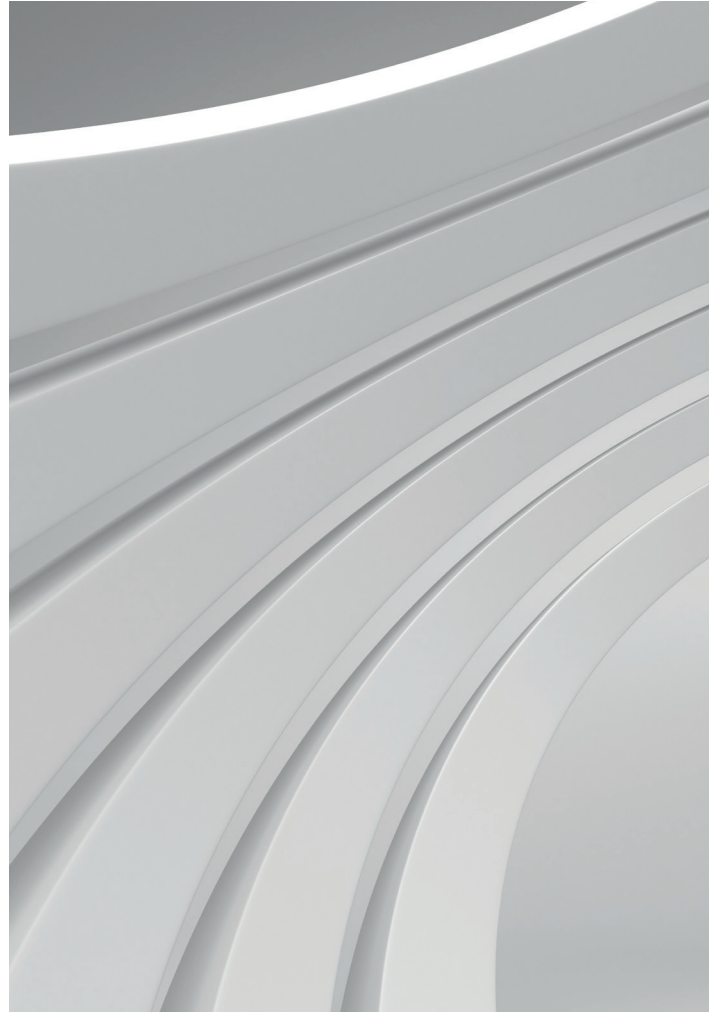
Many firms still align their CCP and OTC clearing operations by asset class. This means they operate separate collateral pools to manage margin. Often, these segregated structures are not positioned to take advantage of CCP margin netting and compression to realise collateral and cost efficiencies and potentially release locked-in collateral for revenue generating opportunities. Align this to the fact that the major CCPs are now partnering with investor CSDs to leverage their tri-party collateral services to cover margin then there are significant opportunities to realise further collateral efficiencies across multiple business lines through more joined-up thinking.



Use of tri-party collateral services

Most of the larger firms utilise tri-party collateral services through either investor CSDs or their larger custodian relationships. Historically, these services have tended to be used to service specific business areas such as securities financing. This may be split further by different business lines. Again, this leads to the management of separate collateral pools with the relevant businesses picking up the costs and missing out on revenue opportunities through sub-optimal management of the firm's collateral inventory. If you put this into a wider business context to include CCP margin calls and settlement liquidity, then there is the potential to utilise your tri-party collateral arrangements to service a wider pool of business needs.

These opportunities allow firms to establish a foundation to build a more strategic outlook to optimise their collateral capabilities by demonstrating that significant benefits can be realised through a more joined-up approach.



What Next?

Rationalisation of key functions within the post trade ecosystem will allow firms to optimise their use and management of collateral to better meet their needs.

Please contact [James Arnett](#) to discuss how Capco can help you develop a post trade optimisation programme.

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