White paper

SWIFT's Post-Trade Survey 2013

Leveraging standards and automation to meet the triple challenges of regulation, cost and risk

Introduction

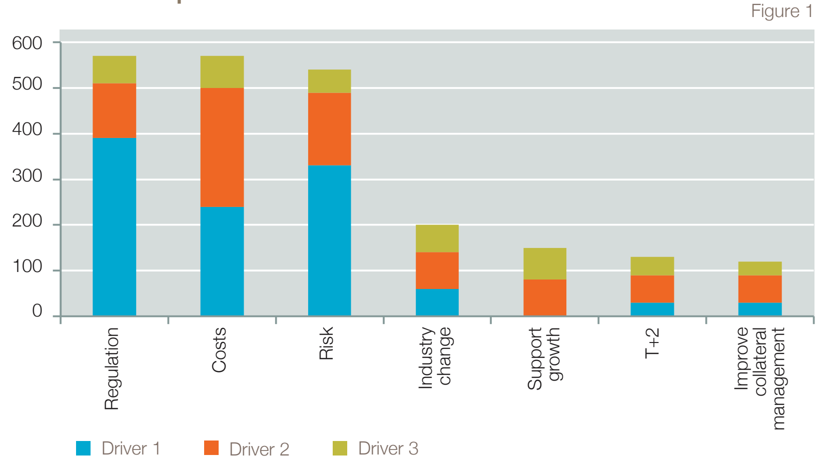
Regulatory change is a major driver for securities and treasury market participants to improve post-trade efficiency. In the current environment this is no surprise. But the results of SWIFT's recent Post-Trade Survey show that the ever-strong imperative to reduce costs is just as powerful a driver for efficiency improvements – and that risk reduction follows closely behind (Figure 1).

Clearly these drivers are inextricably interlinked. On the plus side, efforts to streamline post-trade processing to address one will also serve to address the others. At the same time, the pressure from each driver exacerbates the challenge of addressing the rest.

Improving post-trade automation to meet new regulatory requirements should by its very nature reduce the risk the regulation is designed to combat. It should also yield cost benefits over time. However, it requires upfront investment that is a challenge to fund when – as the survey shows – the majority of respondents expect their budgets for post-trade to either remain the same or decrease in the period to 2015 (Figure 2). Doing more with the same or less is not easy, and indeed the number one barrier to achieving post-trade efficiency goals identified in the survey is 'budget constraints' (Figure 15).

Drivers for post-trade automation

Figure 1



Overall, the survey results give a ringing endorsement to the value of post-trade automation. Respondents confirm that positive affirmation of trades is a major contributor to on-time settlement; 'manual confirmations' are identified as one of the biggest sources of risk in the system; and the availability of a true multi-asset class confirmation matching system ranks as one of the developments that could make the biggest positive contribution to post-trade efficiency.

Budget

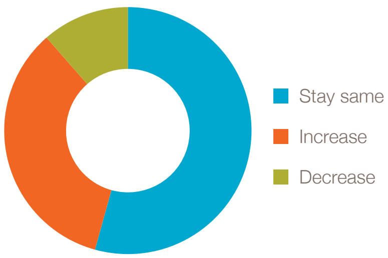


Figure 2

The survey also reveals areas in which more needs to be done, however. These include increasing buy side involvement in industry solutions and achieving more widespread adherence to standardisation and market practice. Only by tackling these issues, the survey results suggest, will the industry be able to ensure that its post-trade processes are robust enough to tackle the triple challenges of regulatory compliance, cost reduction and improved risk management.

Regulation: commanding attention and driving activity

As we have seen, respondents to the survey identified regulation as a top driver for post-trade improvement.

Regulation is not – as might be expected – a runaway winner, however. As Figure 1 shows, regulation was named as number one driver by the biggest number of respondents, but when the first, second and third driver responses are taken into consideration, cost reduction ranks equally highly, and risk is only fractionally behind.

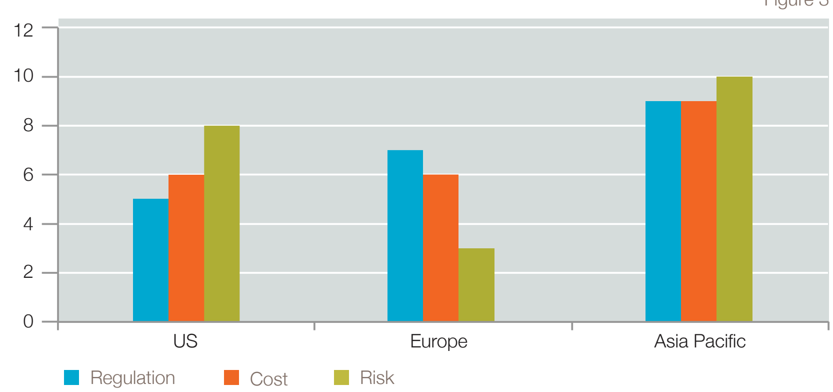
The fine balance between these three key drivers is further evidenced by the survey results broken down according to geography (Figure 3).

That said, the survey results provide ample proof of the major impact the pressure to comply with new regulation is having on the post-trade world.

As Figure 4 shows, the need to regulatory report transactions in response to Dodd Frank/EMIR/MiFID is identified as a top source of operational cost and risk in the post-trade process.

Drivers for post-trade automation

Figure 3

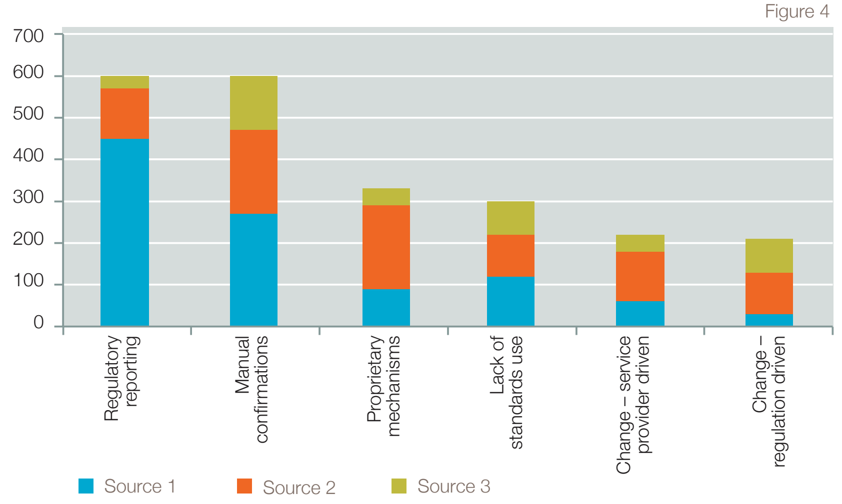


Further, respondents indicate that a number of regulatory requirements are currently commanding the attention of those responsible for post-trade.

Asked to rate their levels of awareness of and readiness for three elements of regulatory compliance with significant impact on post-trade processing – T+2 settlement, electronic confirmation of OTC derivatives and FX/MM and trade reporting – respondents paint a reasonably encouraging picture (Figures 5, 6 and 7). In all cases there are respondents who say that in spite of the acknowledged weight of the regulatory burden, these developments are ‘not on their radar’ from a post-trade perspective. At the same time, the proportion saying this is in each instance outweighed by those who indicate they have made progress of some sort in understanding the post-trade impact of the change, planning and implementing a project to address it and setting aside budget for the project.

Sources of cost and risk

Figure 4



Respondents are furthest along the curve with trade reporting (that they are actively grappling with this challenge is consistent with their identification of this obligation as a major source of operational cost and risk). This could also reflect a tendency to concentrate on events which will impact soonest, although since there has been some movement in reporting compliance dates it will be interesting to see how this evolves.

Similarly, levels of preparedness for the imposition of ETC are encouraging – and again this is consistent with the fact that an equally concerning source of risk and cost for respondents is manual confirmations (Figure 4). Market participants are required to perform ETC under regulation such as EMIR, and the respondents to this survey are also conscious of the cost and risk impact of manual confirmation processing – making this a clear area in which addressing an explicit regulatory requirement also contributes to efforts to manage the perennial concerns of cost and risk.

Respondents are the least advanced with T+2 settlement, though levels of impact understanding are good and we would expect to see activity in this area start to build given some markets have confirmed intentions for a 2014 go-live.

T+2 settlement

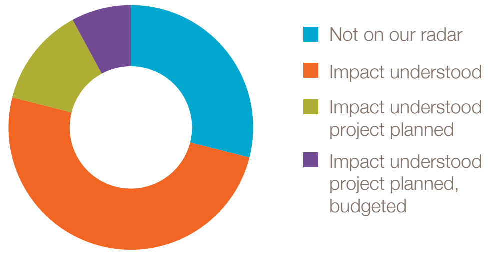


Figure 5

ETC of OTC derivatives/FX/MM

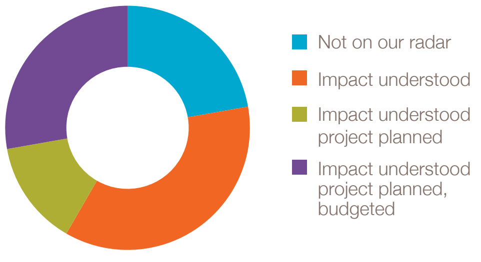


Figure 6

Trade reporting

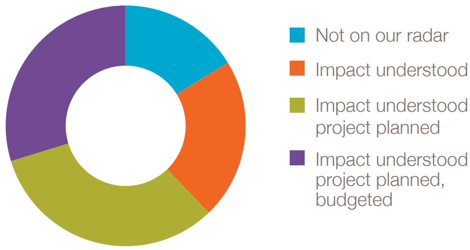


Figure 7

Expected change to post-trade as a result of regulation

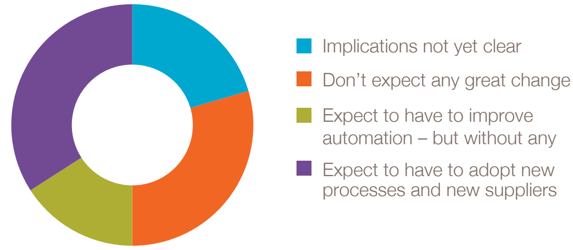


Figure 8

The survey also sought to establish how much change respondents expect complying with regulation will require to existing post-trade set-ups. As Figure 8 shows, the overall proportion expecting the improvements they will have to make to require them to implement new processes and work with new suppliers is significant. Reflecting this global expectation, 35% of respondents from Asia Pacific, 57% from Europe and 66% from the US indicated they anticipate their post-trade automation improvement programmes will be sufficiently thorough to warrant such intervention.

Post-trade automation: viewed as essential, but some gaps remain

The survey shows quite clearly that respondents see the value in automating key aspects of post-trade processes such as affirmation/confirmation. When asked, what impact does positive affirmation of trades have on your settlement rate?, 74 per cent indicated 'positive affirmation causes more than 90 per cent of my trades to settle on time' (Figure 9). Being able to achieve timely settlement is not only essential in light of regulatory moves to shorten settlement cycles, it is also vital from the perspective of operational cost and risk control.

The picture respondents paint of their current affirmation rates across asset classes reveals potential gaps that need to be filled, however. Figures 10 and 11 show the percentages of respondents indicating that more than 75 per cent of trades in a given asset class are positively affirmed with counterparties via central matching and local matching respectively. Because the survey was completed by a range of market participant types with differing levels of involvement in different businesses, it is important not to draw the comparison between affirmation levels across asset class types too far. However we can see that based on the data from this particular sample of participants, cash equity and FX/MM stand out (central match 62%/local match 44% and central match 42%/local match 30%), while the results for other asset classes show lower levels of central or local matching-based affirmation.

Impact of affirmation on timely settlement

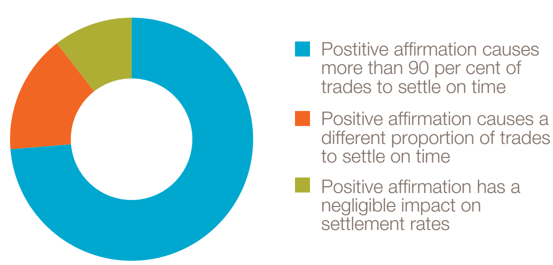


Figure 9

Affirmation rates

Figure 10

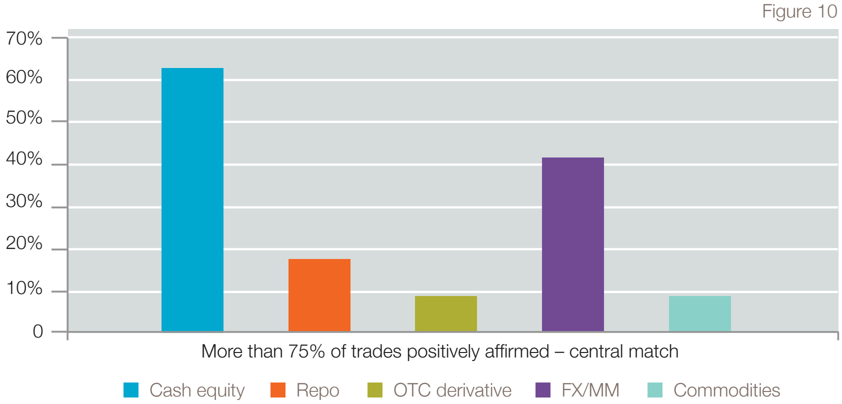


Figure 11

When the results are broken down by participant type we can see that buy side respondents report using an average of 2 systems to automate post-trade flows. The average for broker/dealers and custodians is higher at 3. This is to be expected since received wisdom has it that the sell side of the market needs to support the buy side by making available as many solutions as the buy side wants to use. As investment managers consolidate their processes on fewer systems, broker/dealers and outsourcing providers can be forced to spread theirs out ever more widely. More systems mean more fragmented processes, higher costs and potentially higher risks.

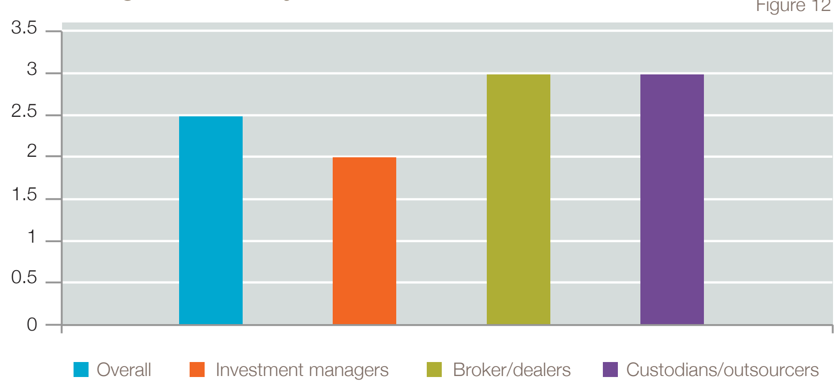
It is worth noting here that this received wisdom is not necessarily consistent with findings elsewhere in the survey. For example, as Figure 13 shows, support for the view that the sell side should be solving the post-trade problem on behalf of the buy side is relatively low.

Since respondents are in no doubt of the positive impact of affirmations on post-trade efficiency, it would seem to be a priority to increase affirmation rates across asset classes. Encouragingly, we know that respondents are engaged in meeting regulatory demand for improved ETC (Figure 5), and that they are aware of the magnitude of the cost and risk problem created by manual confirmations (Figure 4).

The survey results also offer insights into the current use of post-trade systems by respondents. As Figure 12 shows, overall, respondents report that they currently use an average of 2.5 different systems for post-trade processing across asset classes (cash equity, fixed income, repo, OTC derivative, FX/MM, commodities). This result implies that respondents are - on average - having some success in re-using one system/ protocol across multiple asset classes.

Average number of systems used

Figure 12



The role of the buy side

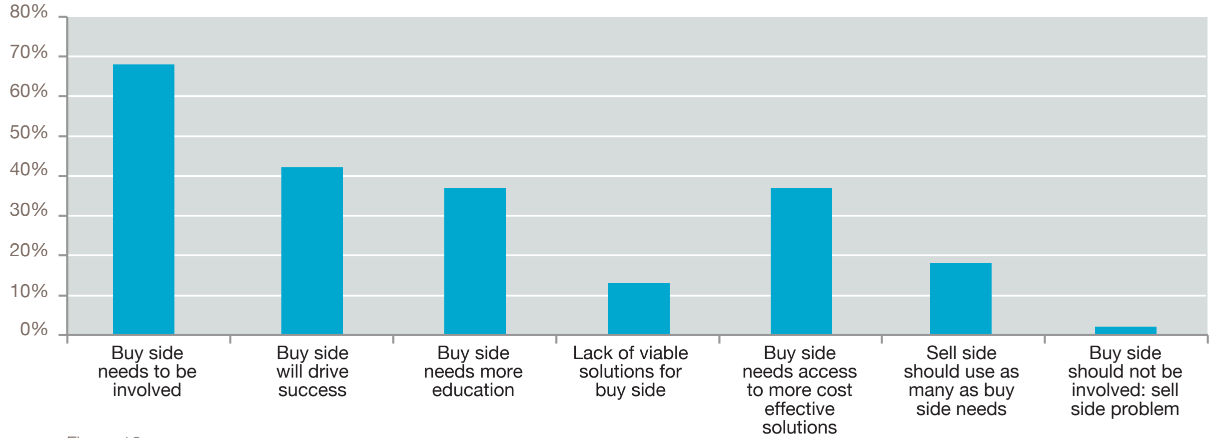


Figure 13

In addition, one of the top responses to the question, 'What single development in the marketplace would have the biggest positive impact on operational efficiency of post-trade flows for the industry?' is interesting to note in this context (Figure 14). Respondents clearly demonstrate demand for a 'true multi-asset class confirmation matching system'.

Overall, the Post-Trade Survey tells an encouraging story about current levels of automation. It tells a stronger story still about levels of ambition to achieve improvements in this area. The findings suggest there is demand for confirmation matching solutions that cover multiple asset classes. The opportunity to rationalize multiple systems down to one would generate efficiencies – and multi-asset class coverage via a single solution could help to raise affirmation levels across the board.

Single development with biggest impact

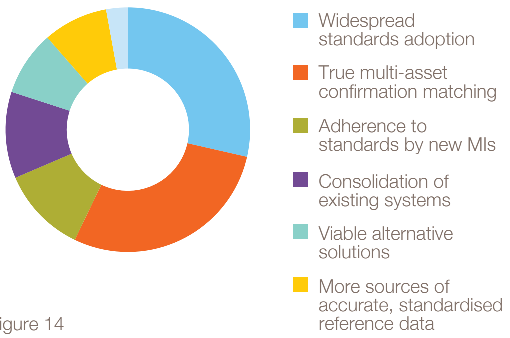


Figure 14

Bringing on board the buy side

Another important piece of the puzzle to enable the industry to achieve its post-trade automation ambitions is securing greater buy side involvement in the process, the survey respondents suggest.

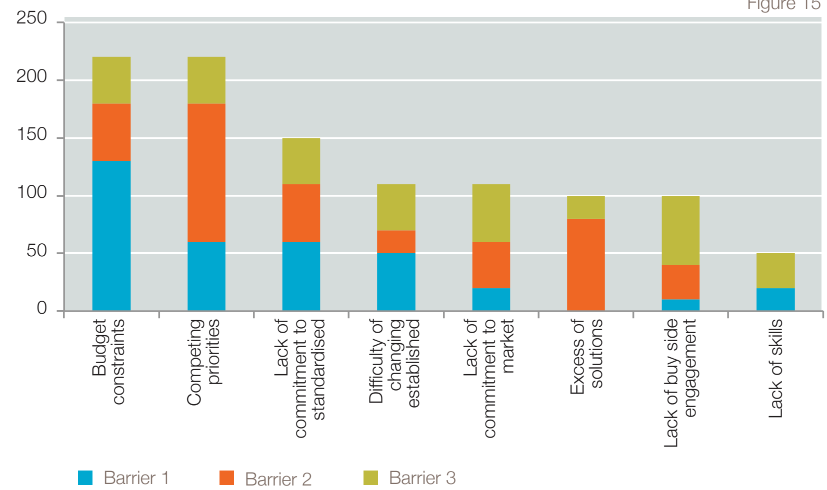
In response to the question, 'What are the biggest barriers you see to achieving improved post-trade operational efficiency in the period to 2015?' (Figure 15), the answer 'lack of engagement by the buy side in industry solutions' was rated 1,2 or 3 by a big enough proportion of respondents to rank it joint fourth. This is not respondents' biggest concern but nor is it negligible.

This finding is consistent with those shown in Figure 13. As already noted, the idea that the sell side can or should solve the industry's post-trade challenges on behalf of the buy side is not widely agreed with. On the other hand, the statement 'The buy side needs to be involved to make industry solutions work' was agreed with by 68% of respondents, while 42% agreed that further, 'The buy side will drive the success of post-trade automation solutions'. To this end 37 per cent of respondents said they believe the buy side needs 'more education on how to drive post-trading efficiency' – and the same percentage said 'The buy side needs access to more cost-effective solutions for post-trade processing'.

Forums that engage the buy side in discussion about how to address post-trade challenges in response to the drivers of regulation and cost and risk reduction – and solutions that make buy side participation easy and affordable – would seem to be good steps towards bridging the buy side gap that concerns some of the survey respondents.

Barriers to achieving post-trade goals

Figure 15



Standards: key to success

As Figure 15 shows, the second and joint third ranked barriers to achieving post-trade efficiency goals in the period to 2015 are 'Lack of commitment to use of standardized solutions' and 'Lack of commitment to use of agreed market practice'.

The concerns respondents express in the area of standards and market practice are consistent with findings elsewhere in the survey. As shown in Figure 4, the second and third sources of risk and cost in the industry are identified respectively as 'Use of multiple proprietary mechanisms to communicate with counterparties/ market infrastructures' and 'Lack of use of standardised messaging in the post-trade process'.

Figure 16 shows how these concerns are reflected across the three regions surveyed: in Asia Pacific, lack of use of standardised messaging for post trade comes out particularly strongly.

Given these findings, it is no surprise that the call for more standardisation to help address post-trade automation challenges is reflected in respondents' answers to the question 'What single development in the marketplace would have the biggest positive impact on operational efficiency of post-trade flows for the industry?' (Figure 14).

The joint 'top answer' from respondents was 'Widespread adoption of standardised messaging for communication' (27%, alongside 'Availability of true multi-asset class confirmation matching solution'). The answer given by 11% was 'Adherence to international standards by new and existing market infrastructures' – reflecting a possible demand from respondents to be able to reuse their investment in standardised communications mechanisms as widely as possible. Since 8% selected 'Additional sources of accurate, standardised reference data', in total almost half of respondents (46%) called for more use of standards in some shape or form.

Leveraging industry standards (using one standardised 'pipe' for communications rather than multiple) and adhering to market practice are both well-recognised foundations for streamlining processes industry-wide while maximising the value of existing investments in automation – a useful attribute in times when budgets are constrained. As a consequence, responding to the demand identified in this survey for greater use of both should yield significant benefits in the quest for better post-trade automation.

Key sources of risk and cost

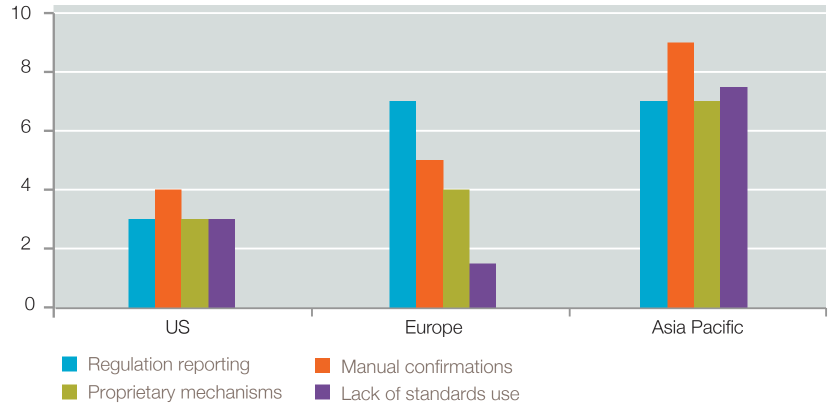


Figure 16

Conclusion: Achieving ambitions while managing constraints

SWIFT's Post-Trade Survey 2013 reveals among respondents a clear interest in improving post-trade automation levels, driven by three major imperatives – regulatory compliance, cost reduction and improved risk management. As we have seen cost is as big a driver for post-trade efficiency improvements as regulation, and risk also features strongly – with these triple challenges combining to increase the pressure to standardise and automate post-trade flows. Indeed the cost pressure is intense, with most respondents expecting at best static budgets with which to effect these improvements.

The survey results suggest a number of positive steps that could be taken to help achieve these post-trade ambitions, meeting regulation and risk challenges while keeping costs under control.

These include efforts to consolidate post-trade flows on to fewer systems, taking advantage of multi-asset class confirmation solutions, extending the use of standardised communications mechanisms and market practice, more successfully involving, and lowering the barriers to entry for, the buy side of the market, and raising levels of affirmations across asset classes and market participant types.

Annex: SWIFT's Post-Trade Survey 2013: background

The online survey was conducted among SWIFT's global securities and treasury community during Q3 2013. This report is based entirely on data gathered from participants through the survey.

Figures 17 and 18 show the geographical and participant type breakdown of the respondents.

Geography of respondents

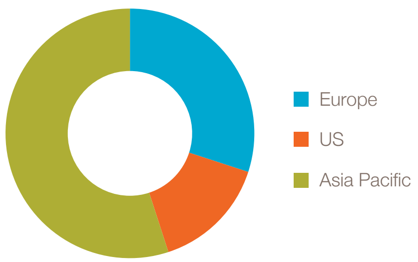


Figure 17

Participant type

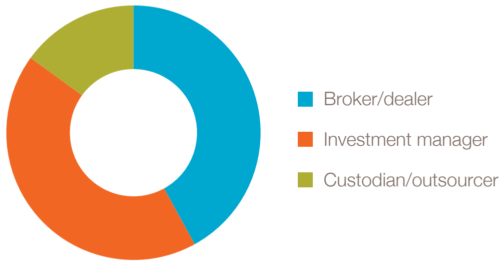


Figure 18

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