

A blurred photograph of a modern office interior with large windows and people walking, serving as the background for the slide.

Settlement Discipline: Assessing readiness for forthcoming regulation

Agenda

- **Opening remarks**
Pierre Davoust, Head CSDs, Euronext
- **SDR implementation in the European Union**
Stella Kaltsouni, Policy Officer at European Commission, DG FISMA
- **Overview on open points, issues and risks**
Sachin Mohindra, Executive Director - Market Solutions, Goldman Sachs
- **Impact of the SDR on the secondary markets**
Andy Hill, Senior Director, ICMA
- **Panel: How market participants are getting ready for the new regulation**
Marcello Topa, Director - EMEA Market Policy and Strategy, Citi
Alex Dockx, Executive Director - Industry Development, JP Morgan
Sophie Janssen, Head of Product Management, BNY Mellon
Michela Rabbia, Head of FI Product – Securities Services, Intesa Sanpaolo
Christine Strandberg, Regulatory Manager – Investor Services, SEB
Moderator: Alessandro Zignani, Head of Business Development, Monte Titoli
- **How Euronext is supporting local markets**
Paolo Carabelli, Manager Settlement and T2S – Product Development, Monte Titoli
Thomas Metier, Head of Business Operations, Euronext VPS
- **Q&A and Closing**

Impact of SDR on the secondary markets

Mandatory buy-ins and the European bond markets

Andy Hill, Senior Director - ICMA

Agenda: Impact of SDR on the secondary markets

- 1. Risks title hereto market-makers**
- 2. ICMA Bond Market Impact study (2019)**
- 3. Bond markets during the Covid-19 turmoil**

Risks to market-makers

The market-maker shows an offer to her client on the basis of being able to borrow and/or source the bonds to make good delivery.



The buy-in will always be executed above market, due to guaranteed delivery and 'signaling'. There could also be a fee charged by the buy-in agent.



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$$\text{Cost} = \text{Buy-in Price} - \text{Re-sale price/Mark-to-market}$$



In the event of a buy-in, the market-maker will incur a cost (the 'buy-in premium'). Theoretically there is no limit to this cost.

Mandatory buy-ins under CSDR and the European bond markets: Impact Study

November 2019

<https://www.icmagroup.org/assets/documents/Regulatory/Secondary-markets/CSDR-Settlement-Regulation/Mandatory-buy-ins-under-CSDR-and-the-European-bond-markets-Impact-Study-271119.pdf>



Mandatory buy-ins under CSDR and the European bond markets Impact Study

An initiative of the ICMA Secondary and/or Primary Committee

November 2019



Impact Study

Scope and methodology of the study

The study sets out to answer five key questions:

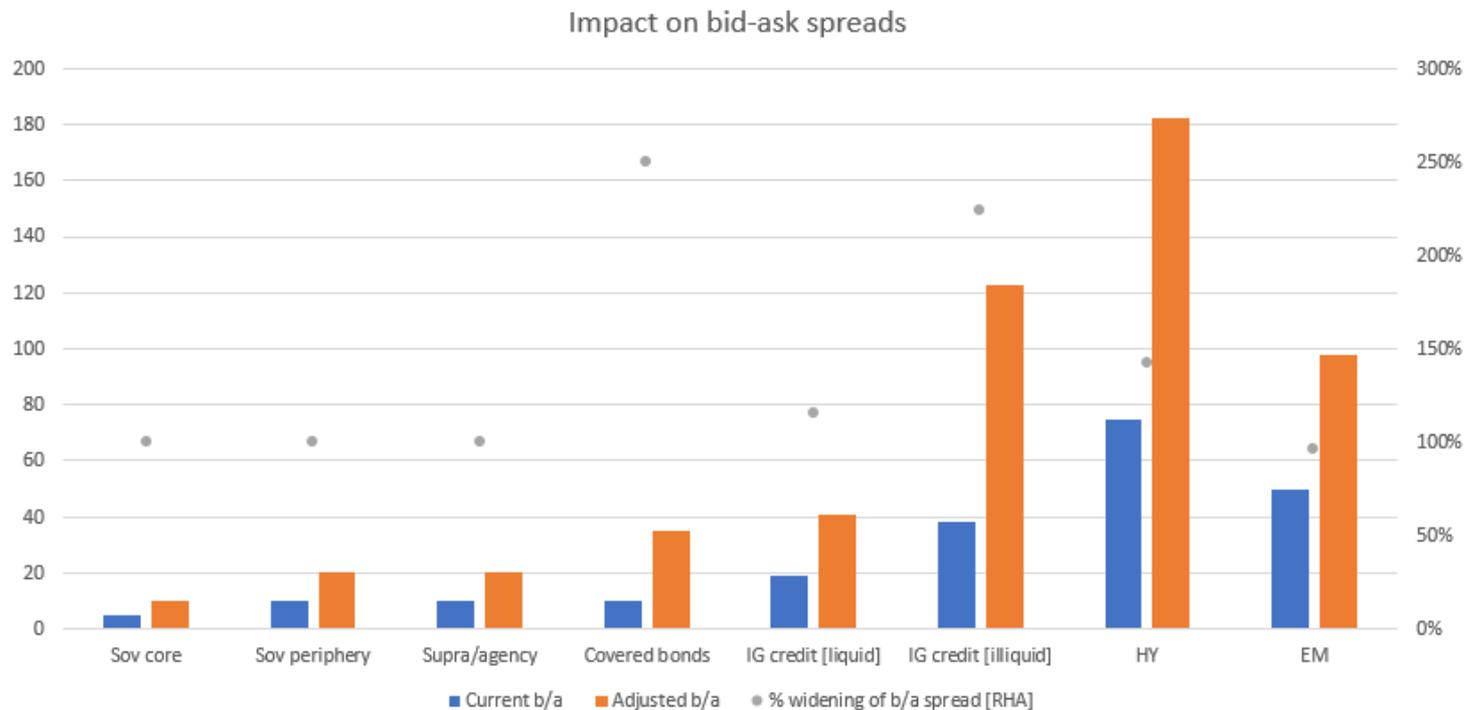
- What is the general preparedness of firms both from an operational and trading strategy perspective?
- How will sell-sides adjust their pricing and liquidity provision across a range of bond sub-classes?
- What are the expectations of buy-sides with respect to pricing and market liquidity?
- What are the likely impacts for repo and securities lending?
- What possible refinements or enhancement to the framework could help to mitigate the risks of unintended consequences?

Online surveys were developed, targeted at three different member constituencies:

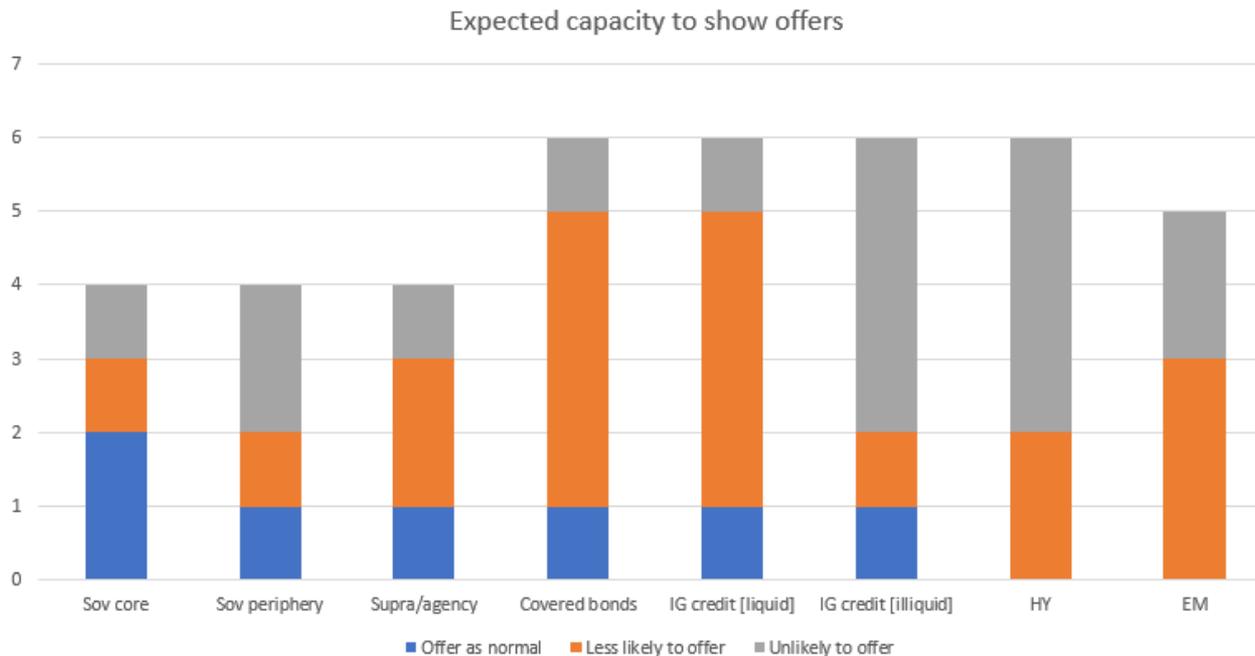
- Sell-side market-makers
- Buy-side investors and asset managers
- Repo and securities lending desks

The surveys received a total of 44 responses. Not all respondents answered every question, and the range of responses for each of the three surveys are spread accordingly: *sell-side (6-16)*; *buy-side (15-16)*; *repo/securities lending (11-12)*.

Sell-side pricing

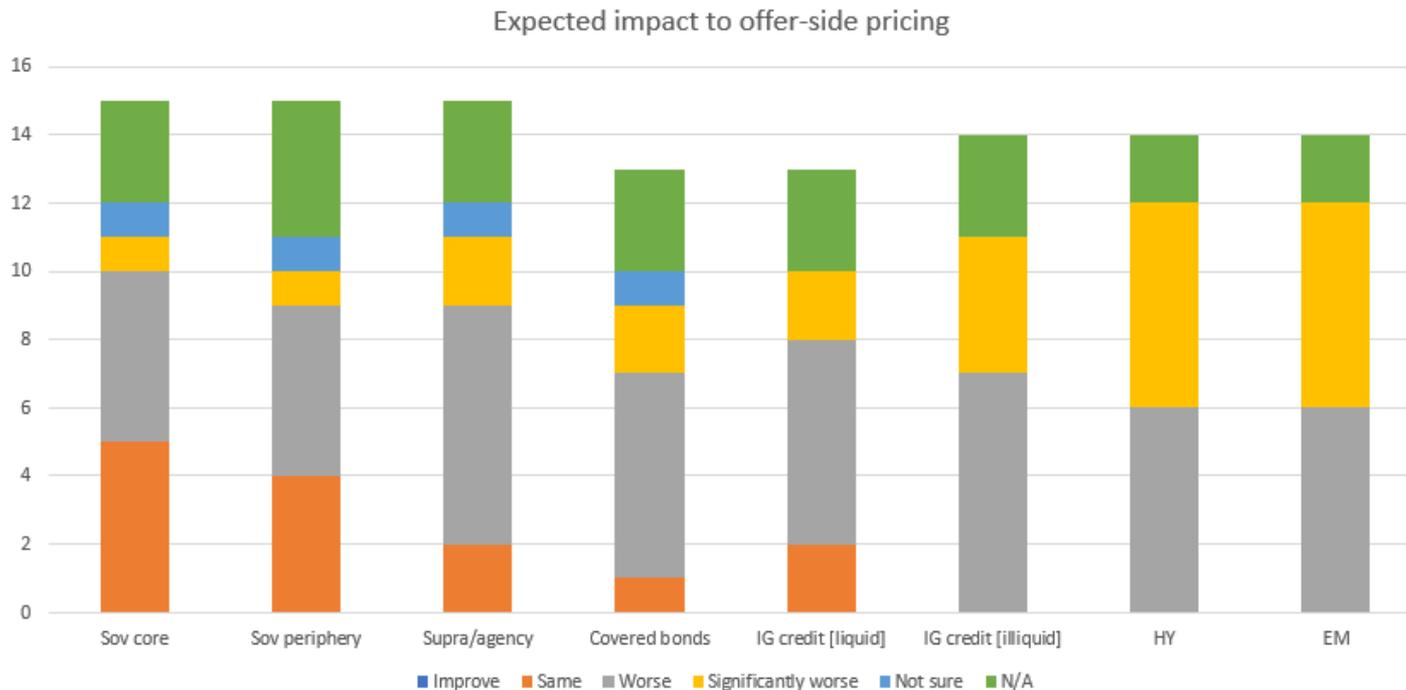


Sell-side liquidity

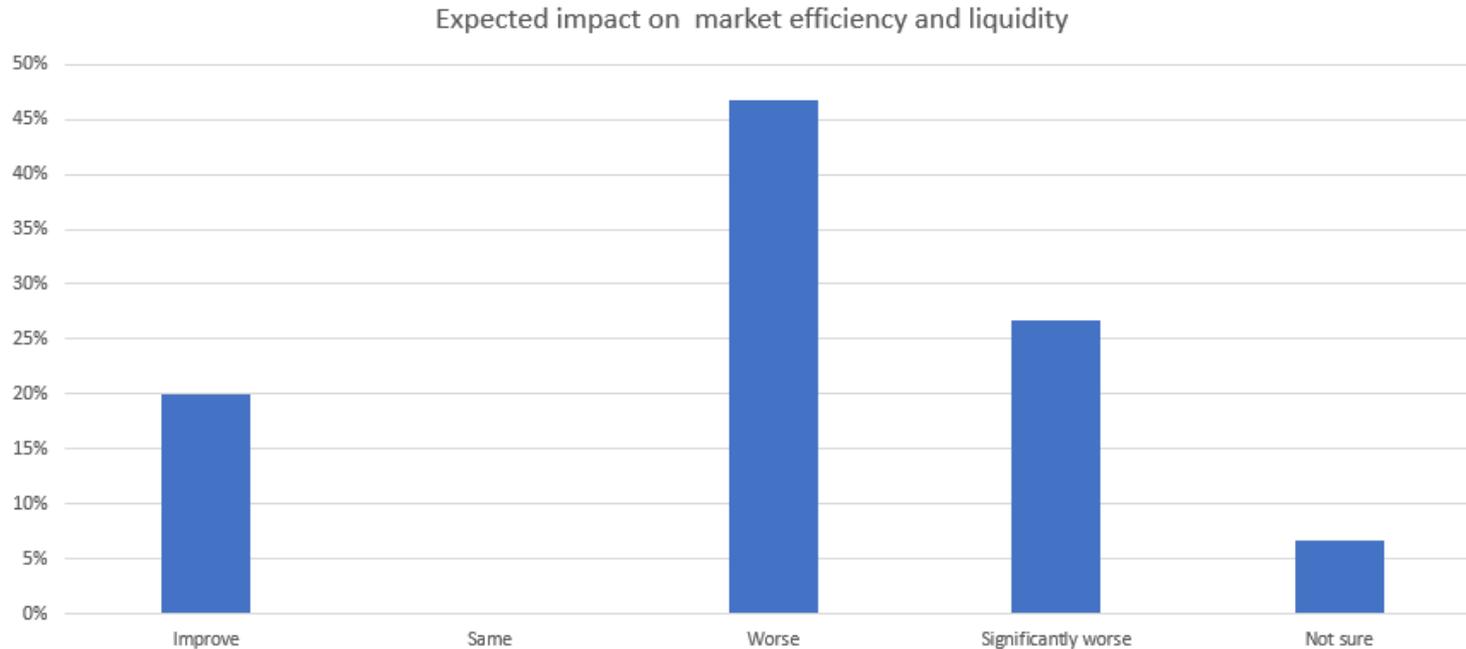


Impact Study

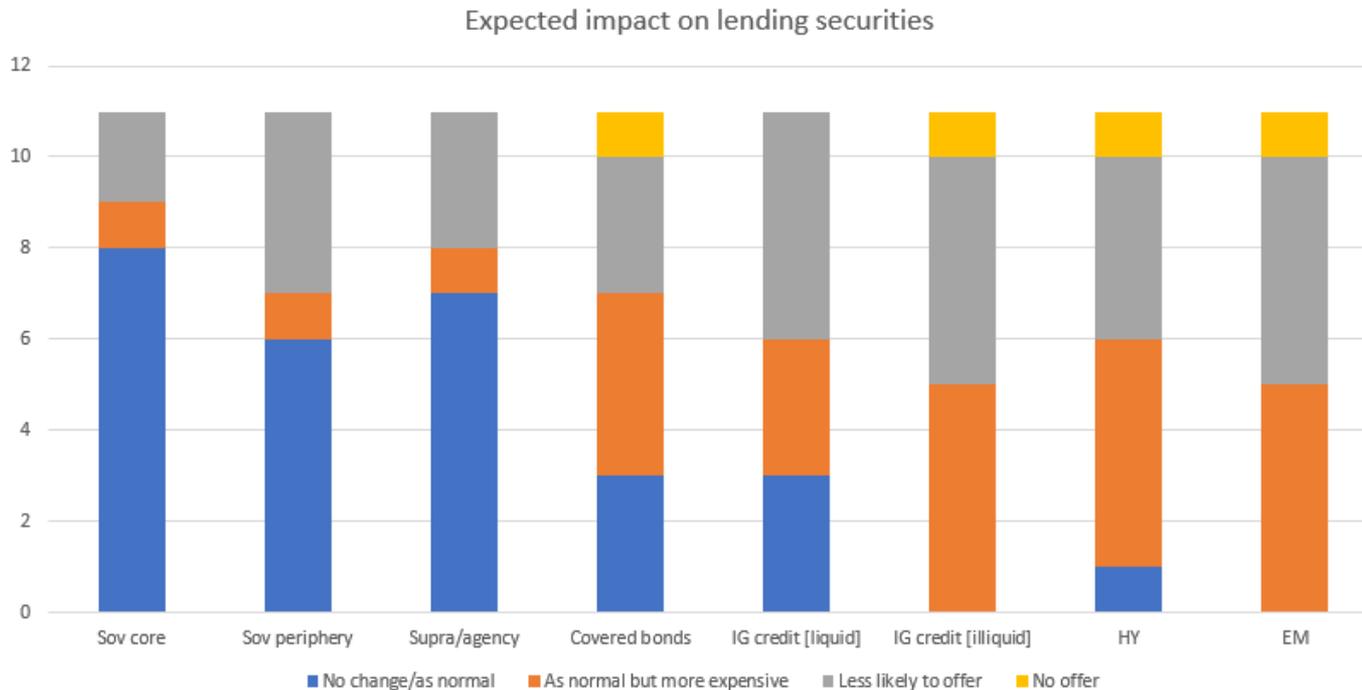
Buy-side expectations



Buy-side expectations



Repo and securities lending



Bond markets during the Covid-19 turmoil

ICMA response to European Commission Targeted Review of CSDR

February 2021

Would the application of the settlement discipline regime during the market turmoil provoked by COVID-19 in March and April 2020 have had a significant impact on the market?

<https://www.icmagroup.org/assets/documents/Regulatory/Secondary-markets/CSDR-Settlement-Regulation/ICMACSDR-Review-Targeted-ConsultationFeb-21Detailed-response-020221.pdf>

European Commission Targeted consultation on the review of the Regulation on improving securities settlement in the European Union and on central securities depositories

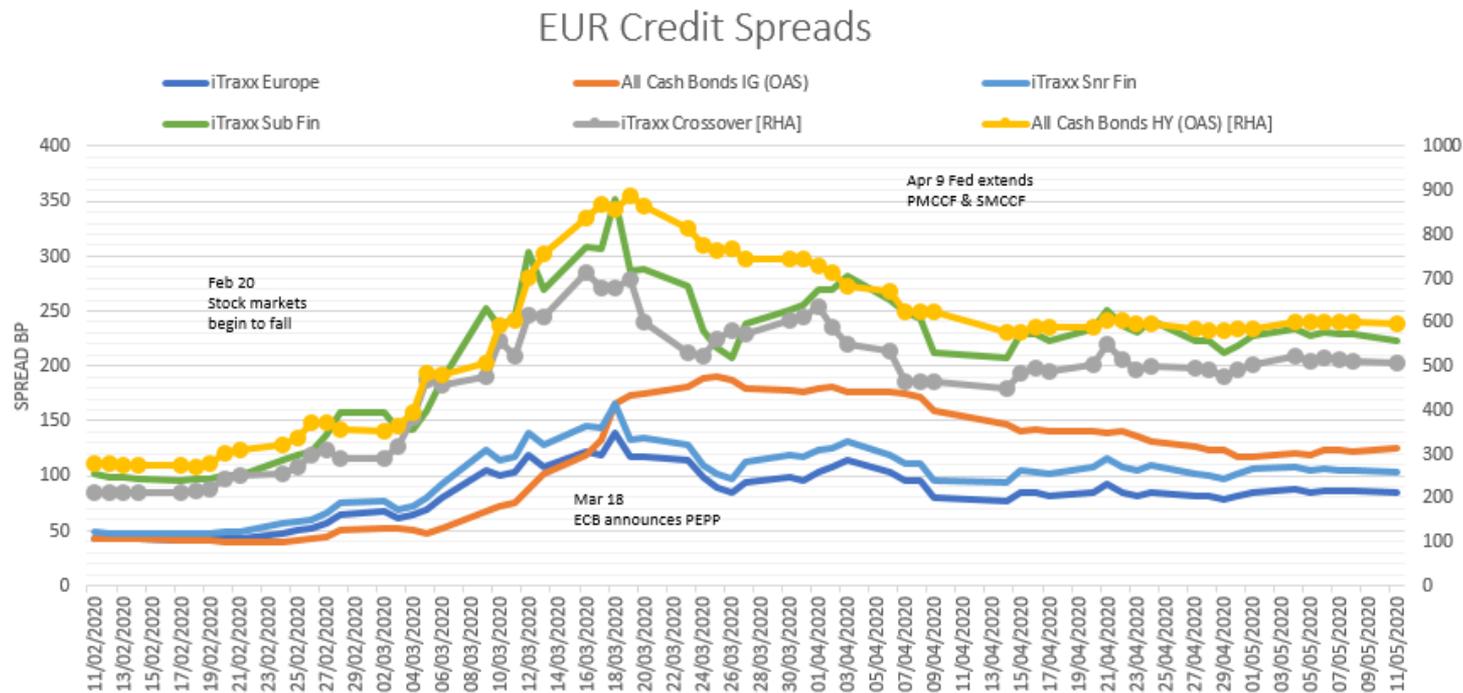
ICMA Detailed Response (February 2021)

Executive summary of the response

- ICMA's response is focused primarily on Settlement Discipline, and from the perspective of non-cleared bond and repo markets.
- Buy-ins, whether regulatory or contractual, should be discretionary and not mandatory. Mandating buy-ins will have adverse impacts for European bond market efficiency and liquidity. The response presents quantitative analysis to illustrate the scale of the costs that market participants (particularly investors) are likely to incur.
- Analysis using settlement efficiency data illustrates not only how extensive and disruptive a mandatory buy-in regime would be for European bond markets under normal conditions, but that the procyclical impacts during the March-April 2020 COVID-19 market turmoil could have been catastrophic.
- In its response, ICMA presents a 'waterfall' of proposals for implementing the Settlement Discipline regime, based on members' assessment of what is most optimal in terms of minimizing disruption to the orderly functioning of Europe's bonds markets, while still attaining the objective of improved settlement efficiency. The suggested, alternative options can be summarized as:
 - (i) implement cash penalties, but not regulatory buy-ins (the need for and design of a regulatory buy-in regime should be subject to a robust market impact assessment); or
 - (ii) mandate that all EU investment firms have in place contractual frameworks to remedy fail; or
 - (iii) implement regulatory buy-ins as a last resort but with a number of critical revisions to the current framework.
- If buy-ins are to remain part of CSDR, this will require a number of revisions, including: (i) symmetrical payments for the buy-in and cash compensation differential; (ii) the introduction of a pass-on mechanism; (iii) greater flexibility in the requirement to appoint a buy-in agent; (iv) a clarification (and narrowing) of scope; (v) a more workable cash settlement ('cash compensation') mechanism for illiquid bonds; (vi) more tailored timelines for completing the buy-in; and (vii) guaranteed delivery for the buy-in process.
- ICMA's members are concerned about the current implementation schedule for the buy-in regime, the timetable for any revisions, and the resulting costs and disruptions to the industry of introducing changes midflight. They strongly believe that the buy-in regime should accordingly be delayed.

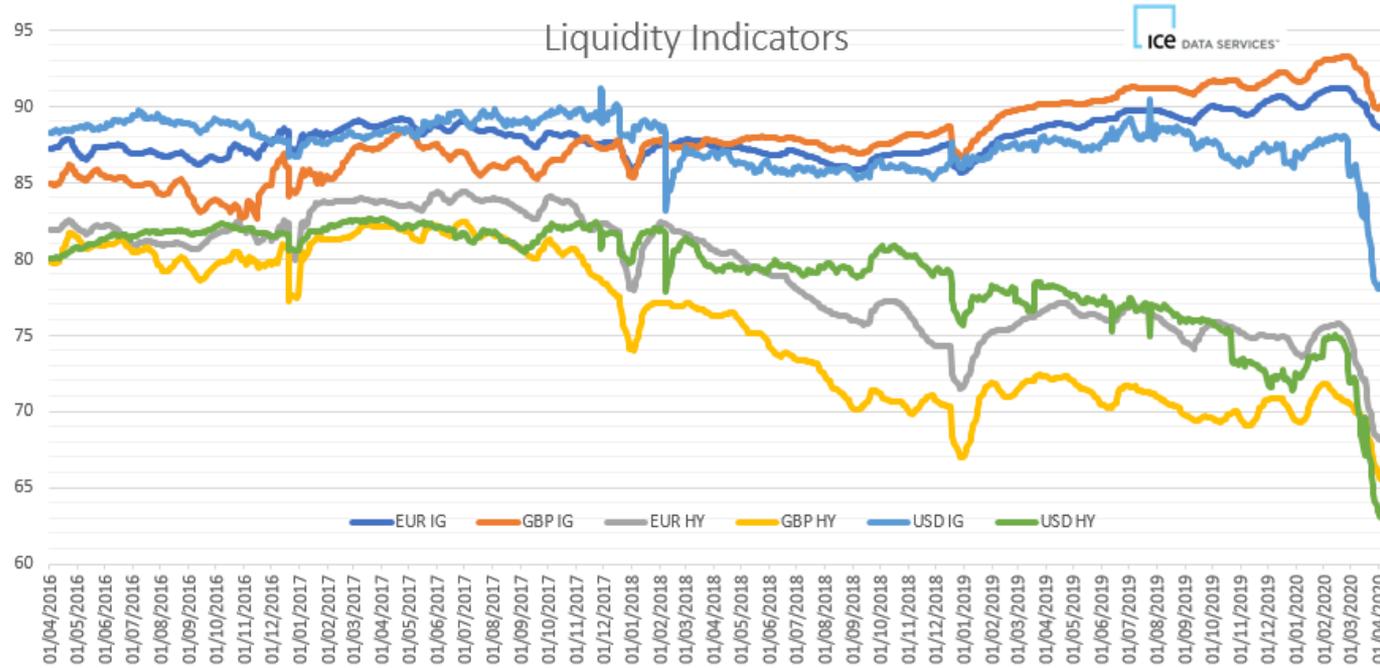
Covid-19

EUR credit spreads



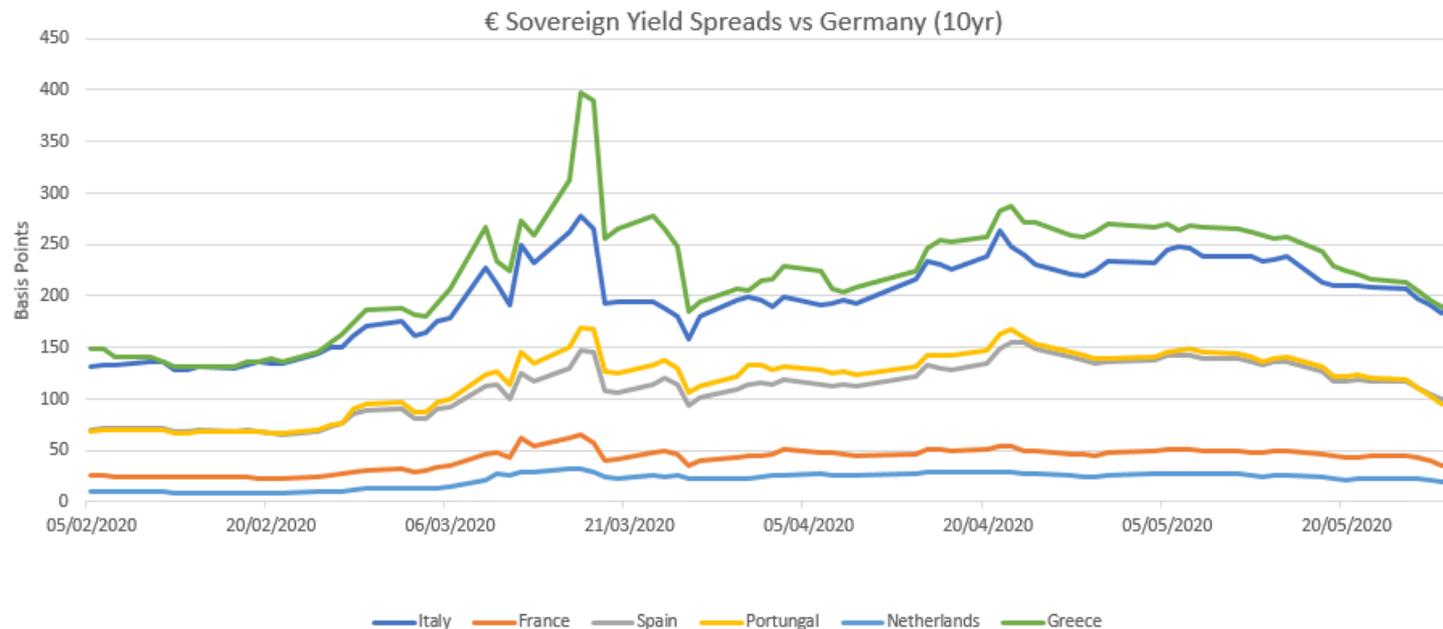
Source: ICMA analysis using Bloomberg data

Corporate bond liquidity indicators



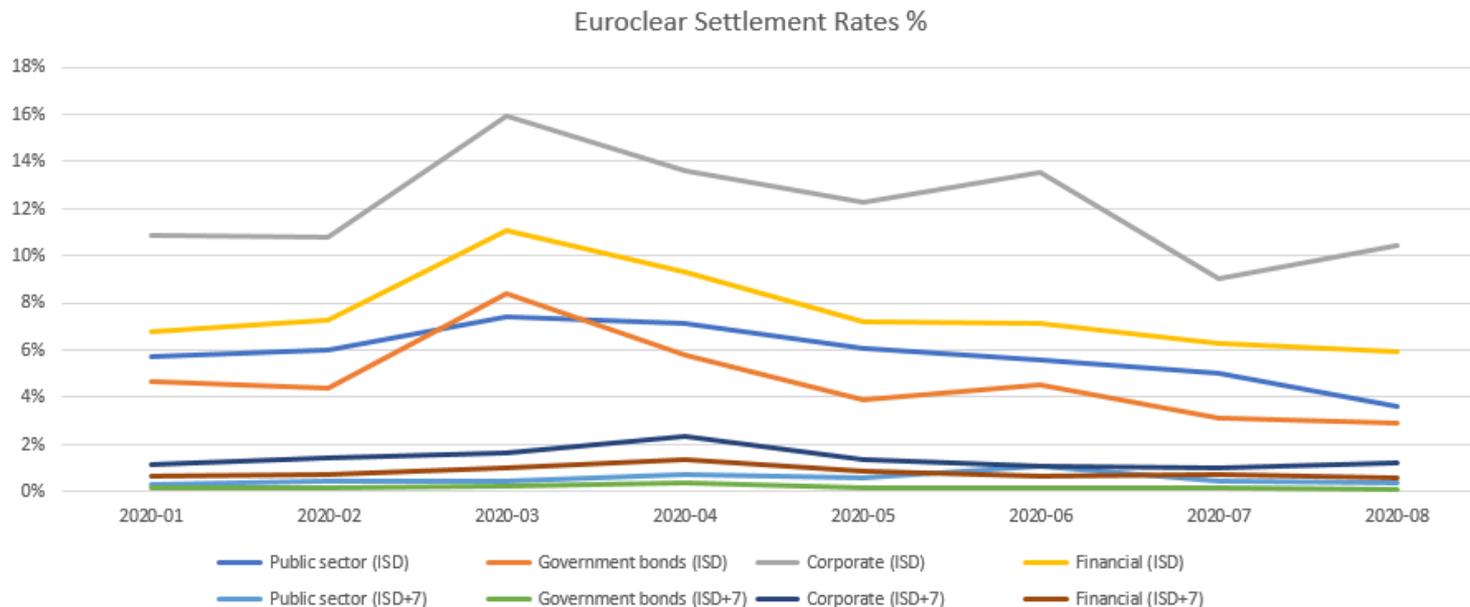
Source: ICE Data Services

EUR sovereign spreads



Source: ICMA analysis using Bloomberg data

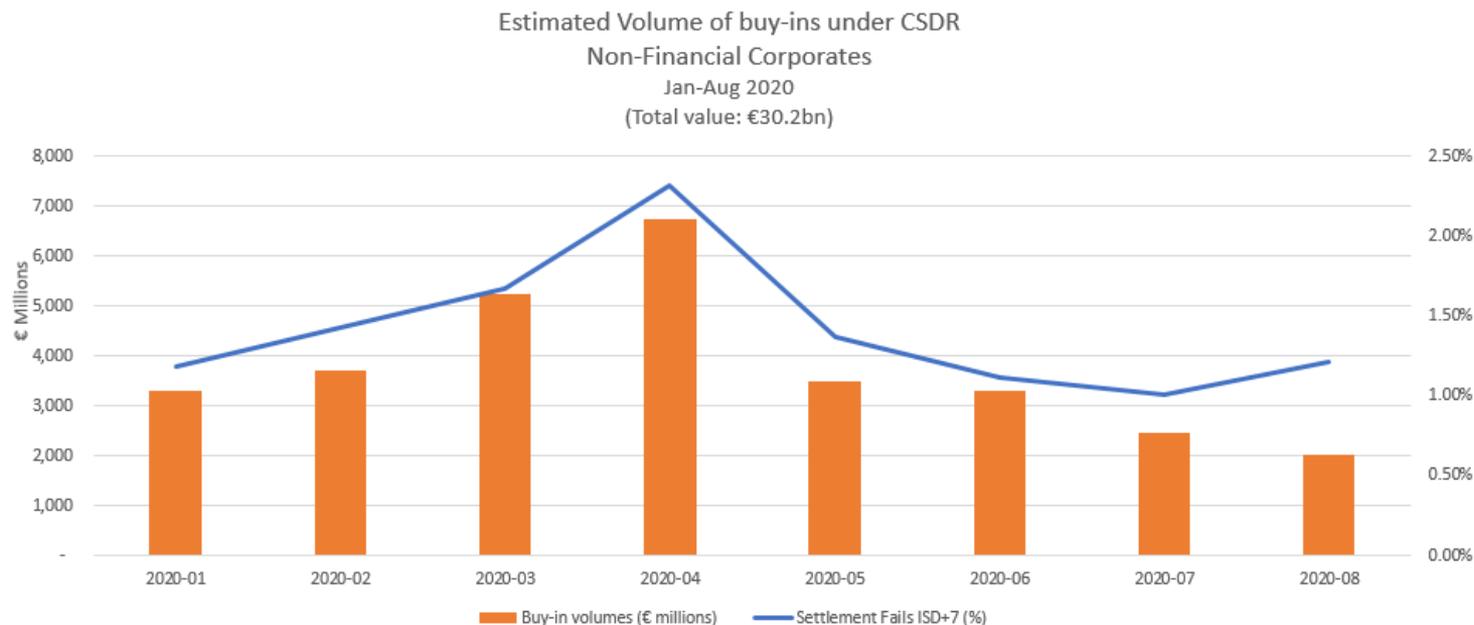
Euroclear settlement rates (FI)



Source: ICMA analysis using Euroclear Bank data

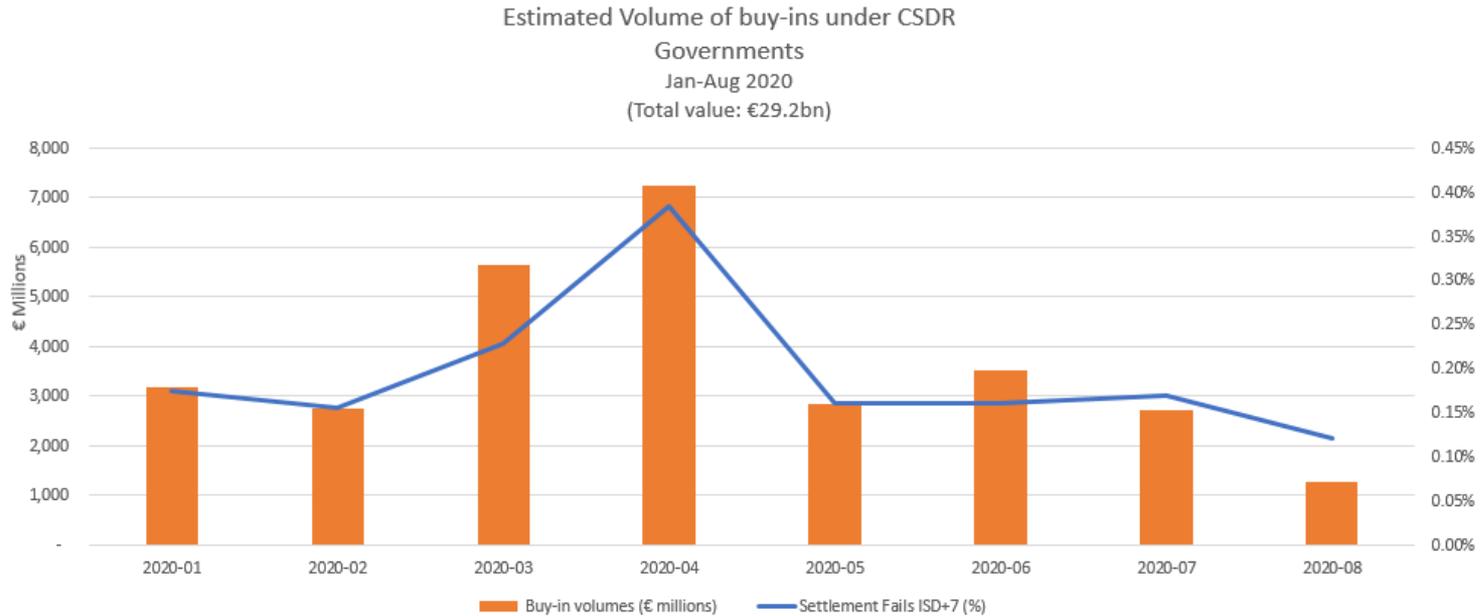
Covid-19

Estimated buy-in volumes (NFCs)



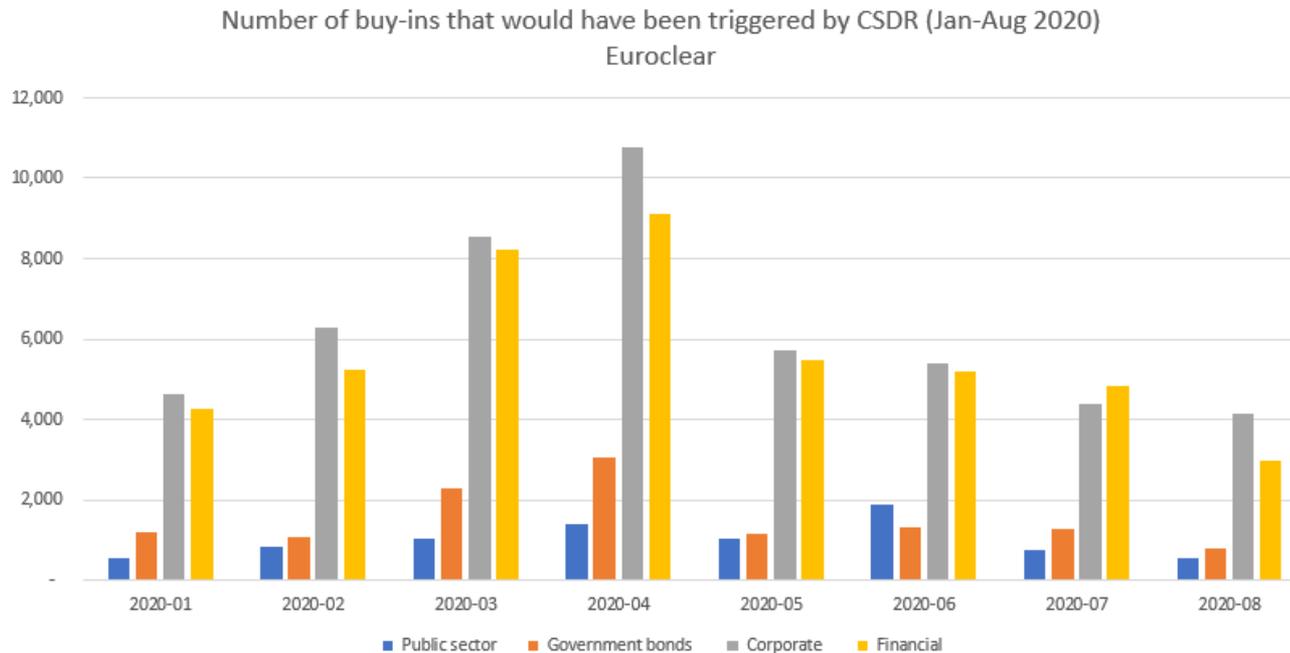
Source: ICMA analysis using Euroclear Bank and Bloomberg data

Estimated buy-in volumes (Sovereigns)



Source: ICMA analysis using Euroclear Bank and Bloomberg data

Estimated FI buy-ins on Euroclear



Source: ICMA analysis using Euroclear Bank data

Thank you

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EURONEXT

How Euronext is supporting local markets

Settlement Discipline Webinar, 7 July 2021

CSDR - SETTLEMENT DISCIPLINE

The new settlement discipline defines the measures to prevent and address settlement fails.

Measures to prevent settlement fails CSDR Art. 6

Automated settlement and fully automated, continuous real-time matching (harmonised matching fields)

Mechanisms for participants to manage settlement instructions

Bilateral cancellation

Access to relevant information

Hold and release

Recycling

Partial settlement

Measures to address settlement fails CSDR Art. 7

Monitoring, reporting and disclosure of settlement fails

Penalties

Buy-in / cash compensation

Suspension of participant

The CSDs of ENX work on every aspect of the settlement discipline

CASH PENALTIES

ENX of CSDs is committed to apply the ECSDA framework.

To whom the ECSDA Framework will apply?

Objective:

Harmonisation of rules and procedures. Focuses on the penalties related questions of the settlement discipline regime of the CSDR

Principles to be applied by all EU CSDs:

- ✓ Provision of a cash penalty mechanism
- ✓ Cash Penalties:
 - Daily calculated, after intended settlement date (ISD) until the actual settlement or cancellation
 - Apply to: matched settlement instruction (free or against payment) that fails to settle after its ISD, including Hold instructions and late matching fails

Daily information to Participants

Collection before redistribution

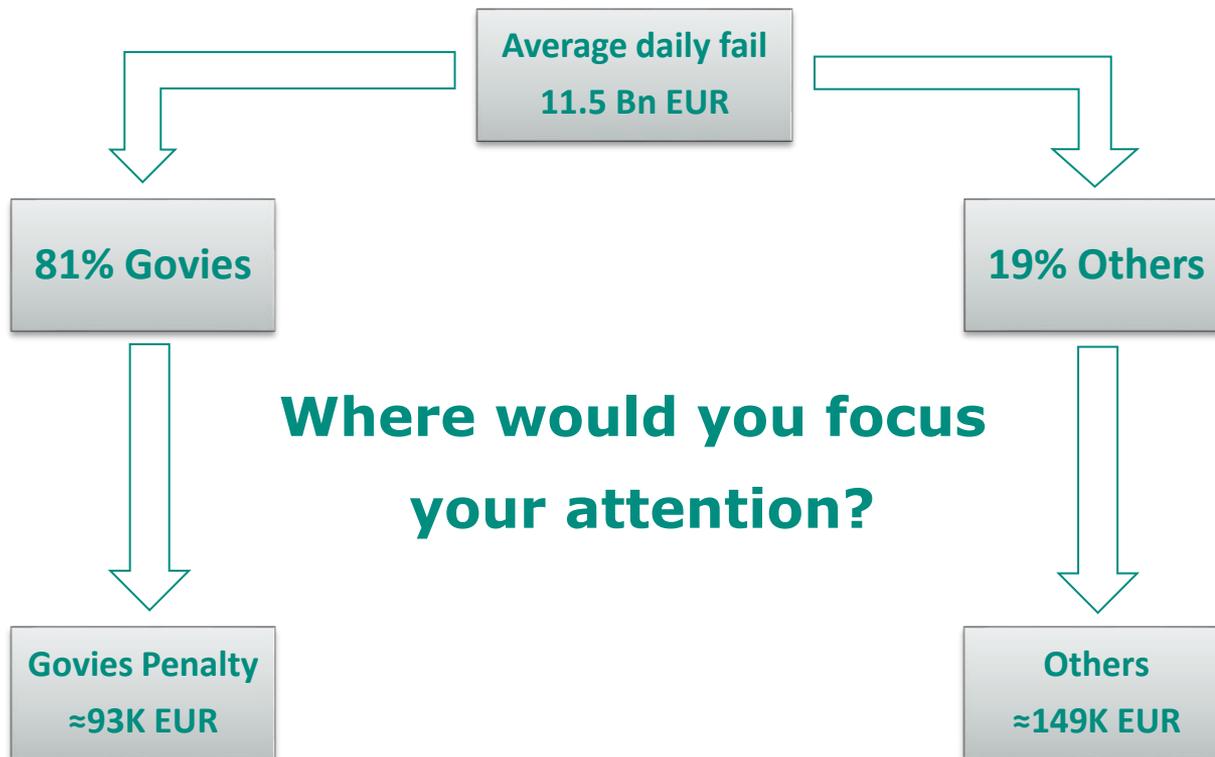
Special situation of the CCPs

Penalties not a revenue source for the CSD

Redistribution of the penalties collected to the participant that suffered from the fail at least on a monthly basis

CASH PENALTIES – The Monte Titoli case

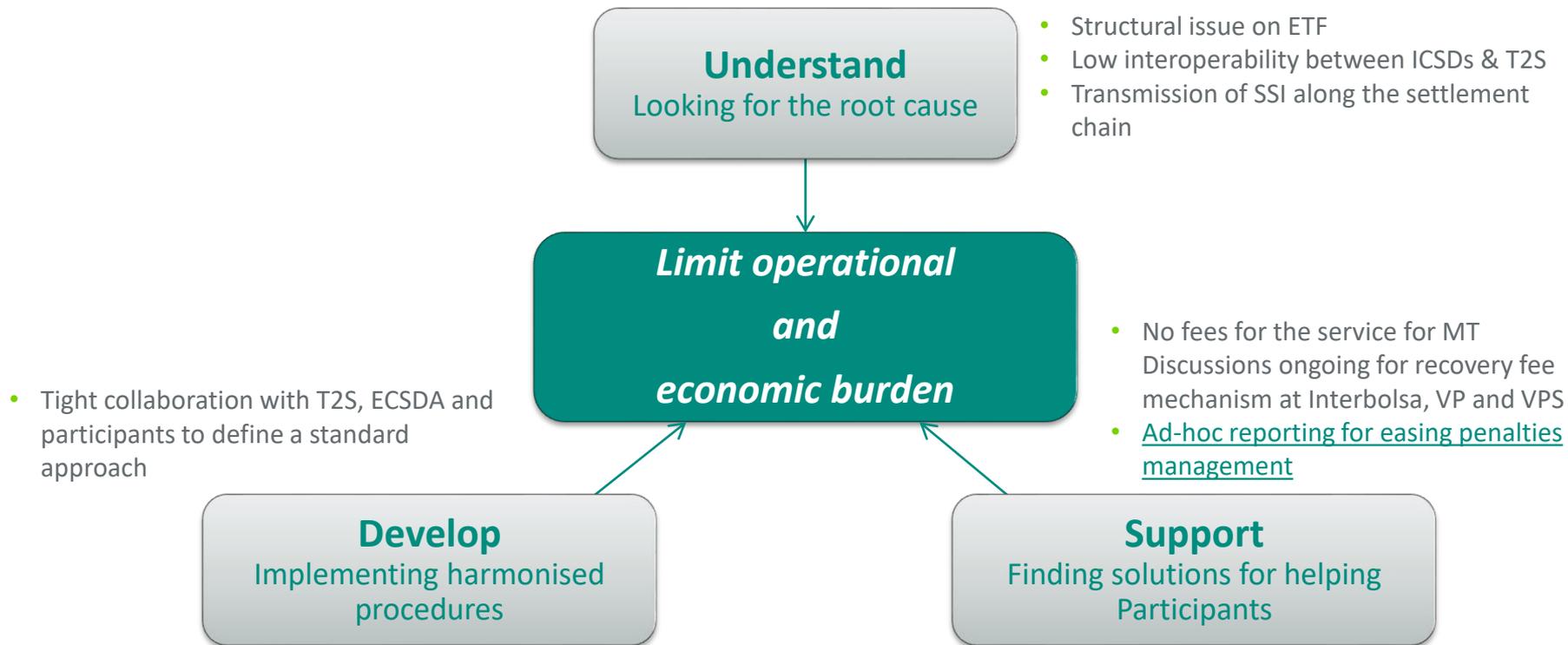
The overall penalties amount around 50 Mio EUR per annum



ETF Penalty ≈66K EUR
SHR Penalty ≈83K EUR

What has been done so far

The ENX of CSDs have worked with their local ecosystems to minimize impacts



What we have to do

The remaining actions until Feb 1, 2022 are well identified and properly monitored.



- ❑ Start user testing and complete a first basic review of the processes (focus on communication)
- ❑ Take advantage of dry-run to effectively assess your readiness, above all in the payment process
- ❑ Solve open-points, such manage contingency situation while processing payments



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Data analytics in practice

Service Quality indexes Bank X



ACB - Anonymous Clients Benchmarking

- Comparing your performance with peers
- Analysing your behaviour per Asset Type and/or Accounts
- Understanding your costs for settlement

SPR - Settlement Penalty Reports

- Controlling cumulative economic impacts of fails
- Timely alerting of buy-in activation
- Monitoring significant fails per Assets class

