

Chapter 18

Undressing the Global Derivatives Market: Trade Repositories: Past, Present and Future

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ABSTRACT

Trade repositories are market infrastructures collecting and maintaining the records of over-the-counter (OTC) derivatives transactions for a large number of asset classes. They have been under the spotlight since the G20 meeting in Pittsburgh and have recently gained very high importance in the field. Reporting obligations have started or will be coming into force in the near future worldwide. The purpose of this chapter is to describe the history and landscape of trade repositories, to outline advantages of having these market infrastructures in place and to briefly review the literature available based on data stemming from trade repositories.

INTRODUCTION

Trade repositories are the youngest financial market infrastructures, yet they have gained very high importance in relatively short time. From their introduction to the wide audience in 2009, trade repositories have been established in every major economy in the world and their data scrupulously safeguarded is now being chased by regulators, supervisors and researchers alike. But what is really a trade repository and what can be done with the data it contains?

The purpose of this chapter is threefold: first, it describes the history of trade repositories and their landscape for the main financial jurisdictions worldwide (Europe, United States and the main economies in the Asia Pacific region), also highlighting the pros and cons of the established frameworks. Second, it outlines some of the advantages of increased transparency in the OTC derivatives markets for counterparties, regulators and academics.¹ Finally, it reviews the literature available based on trade repository data, usually focusing on Credit Default Swap (CDS) contracts recorded in the Depository Trust and Clearing Corporation (DTCC) as early as 2006.

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THE HISTORY

A trade repository is a market infrastructure collecting and maintaining the records of over-the-counter (OTC) derivatives transactions for a large number of asset classes, comprising (i) credit, (ii) interest rate, (iii) equity, (iv) foreign exchange, (v) commodity, (vi) and other derivatives. A trade repository is thus a large-scale database of OTC transactions that should overcome the inherent opacity of OTC derivatives markets thus increasing market transparency. Trade repositories will help public authorities and market participants in monitoring market developments more closely and analysing specific issues in depth, such as build-up and distribution of exposures in any market segment.

The first market infrastructure similar to a trade repository, the Trade Information Warehouse (TIW), was launched in November 2006 by DTCC in collaboration with market participants. From its original aim of centralizing the maintenance and automated processing of OTC derivatives contracts, TIW expanded its functionalities in November 2007 by adding a central settlement engine for calculating, netting and issuing payments between counterparties becoming, by default, the storage facility for every automatically confirmed trade. That means it also served as an electronic central registry for CDS traded by the largest majority of global derivatives dealers in more than thirty countries.

DTCC and TIW came under the spotlight in the aftermath of the bankruptcy of Lehman Brothers:² market rumours suggested that \$400 billion on CDS naming Lehman Brothers would have changed hands and investors' fear reached a peak when markets closed on Friday 10 October 2008 (Bodson, 2013). However, TIW data reported about \$72 billion in CDS written on Lehman Brothers and registered in the trade repository. In just over a month, the payment obligations arising from these trades were calculated, netted on a bilateral basis for a total amount of approximately \$21 billion and sent to CLS for final settlement on a multi-lateral net basis with other foreign exchange trades for a final amount just over \$5 billion, a reduction of more than 90% from the initial bilateral exposure. The data held in TIW helped calming the global financial markets and facilitated the netting process. Soon after, in November 2008, DTCC began disclosing weekly data on outstanding gross and net notional values for the top 1000 underlying CDS single-name entities and all indices. It represented the first public release of CDS data and enhanced market transparency on this particular asset class. The concept of the Trade Repository was thus born!

However, it was only in late 2009 that trade repositories became worldwide known to market participants, central bankers, regulators and financial journalists alike. In the 24-25 September 2009 summit in Pittsburgh, the G20 leaders agreed that all standardized OTC derivatives should be cleared through central counterparties (CCPs) and reported to trade repositories. The Trade Repository machine was thus started. The goal of the regulators was to enhance market transparency, helping public authorities and market participants to monitor more closely market developments. Several consultation rounds between the Committee of European Securities Regulators (CESR), the Bank for International Settlements (BIS), central banks and market participants worldwide followed. Ultimately, the Financial Stability Board (FSB) and its OTC Derivatives Working Group (ODWG) were mandated to monitor progress and compliance with the commitments set in the Pittsburgh meeting.³ Meanwhile, new trade repositories for equity derivatives, interest rates swaps, commodity swaps and foreign exchange swaps were gradually introduced across the world.

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