POST-TRADING ROADMAP

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The post-trade space is ever evolving

With several workstreams going on and new challenges arising, levels of excitement in the post-trading space are gathering pace! Harmonisation in securities post-trade processes and in collateral management continues as it constitutes a *conditio sine qua non* for an integrated European financial market, while new areas require our attention as well.

The Eurosystem's Advisory Group on Market Infrastructures for Securities and Collateral (AMI-SeCo) has made significant progress in the past years by agreeing on standards for European markets and committing to their implementation. AMI-SeCo is a market stakeholder forum sponsored by the Eurosystem (i.e., the ECB and the National Central Banks of the countries that have adopted the euro), bringing together central securities depositories, central counterparties, banks, central banks, issuers and industry associations and covering the European Economic Area, UK and Swiss markets.

An integral part of AMI-SeCo's work is monitoring and reporting on the progress of implementation of agreed standards:

- AMI-SeCo and its predecessor, the T2S Advisory Group, have monitored compliance by T2S markets with the T2S harmonisation standards for more than 10 years (TARGET2-Securities - T2S – the Eurosystem-operated settlement platform). The overall level of compliance with the T2S standards is around 90% by now, with only a few remaining non-compliance cases.
- The 7th AMI-SeCo SCoREBOARD reporting the progress in implementing the Single Collateral Management Rulebook for Europe (SCoRE) Standards was published in December 2023. SCoRE Standards cover Triparty Collateral Management, Corporate Actions and Billing Processes (while AMI-SeCo aims to define further SCoRE Standards). Although significant progress has been achieved overall by the monitored actors, several markets reported delays. The rescheduling of the Standards implementation date to November 2024, in line with the go-live date of the Eurosystem Collateral Management System (ECMS) which also builds on the SCoRE standards, allows more time for the markets to prepare.
- AMI-SeCo published the 2023 Corporate Events Compliance report which provides an assessment of the current levels of compliance with European corporate events standards, i.e. Market Standards for Corporate Actions Processing, Shareholder Identification and T2S Corporate Actions Standards. The monitoring exercise shows some advances in compliance. Many markets have concrete plans to improve compliance, with the SCoRE Standards and ECMS-readiness acting as a catalyst. In 2024, AMI-SeCo will initiate preparatory work on the creation of a single rulebook for corporate events which will further consolidate the existing separate sets of standards in this domain.

AMI-SeCo is also taking stock of the remaining barriers to post-trade integration and cross-border access. The findings will form the basis of future AMI-SeCo harmonisation/market integration initiatives as well as potential recommendations by AMI-SeCo to European or national law-makers and regulators.

Other authorities are also active in the post-trading domain. In this regard, the Eurosystem welcomes the increasing regulatory and market focus on settlement efficiency led by the European Securities and Markets Authority (ESMA) as well as the investigations into the reasons for settlement fails and possible measures for preventing settlement fails.

Understanding the root causes of settlement fails and ways to prevent them is also essential for any discussion on European securities markets moving to a shorter settlement cycle. It needs to be ensured that, if such a move were decided, it would not lead to a deterioration of settlement efficiency levels. Overall, the question of a potential shortening of the settlement cycle is multidimensional and requires analysis on the basis of market evidence.

Harmonisation continues while new areas require our attention as well.

New technologies are adding another interesting dimension to the post-trade field and the Eurosystem is actively examining how central bank money settlement in euro could take place in the presence of technologies such as Distributed Ledger Technologies (DLT). The Eurosystem is rolling out its exploratory framework with market participants on the use of new technologies for central bank money settlement. Within this framework the Eurosystem will allow eligible market stakeholders to experiment and/or trial (with real-life transactions), settlement of assets or payments against euro central bank money based on new technologies. This work will also help to meet demand for central bank money settlement during the market's own pilots (for example under the EU DLT Pilot Regime) and is considered part of the Eurosystem's contribution to the further digitalisation of finance within the EU. Harmonisation and integration also remain key themes within this new workstream.

Exciting times lie ahead!

MONTSERRAT MARTINEZ PARERA
Vice Chair - Spanish Securities and Exchange Commission (CNMV)

Shortening settlement cycles: is T+1 the way to go?

Ten years ago, European markets transitioned to the current T+2 cycle from T+3, requiring all transactions executed on trading venues to be settled in two business days. It was a significant undertaking across EU securities markets. Since then, settlement efficiency has improved notably, particularly after the disciplinary measures introduced in 2022. However, the improvement has not been even across all jurisdictions and assets classes, and it still can be strengthened.

The recently adopted CSDR Refit is precisely envisaged to tackle certain issues related to settlement failures. This is important. Settlement efficiency plays a critical role in the execution of financial transactions, ensuring both certainty and timeliness, which keep counterparty credit risk under control. Indeed, reducing settlement fails to a minimum will enhance the functioning and competitiveness of the European capital markets. ESMA's recently published consultation paper aims precisely to contribute to this goal by enhancing settlement discipline measures.

However, there are two additional main trends to consider within the settlement business: the steps being taken by some jurisdictions to further shorten the window cycle towards T+1 and the potential of new technologies (distributed ledger technology (DLT) to revolutionize the settlement process.

Both trends point towards an acceleration of the settlement cycle, but I will focus on the former. Questions arise whether Europe should follow this path, and if it does, what benefits it would bring to the European markets. Answering these questions is not straightforward, and the implications need to be carefully weighed.

On the one hand, reducing the settlement cycle could reduce liquidity needs and counterparty exposure thereby reducing margin and collateral requirements. These associated savings in margins are usually presented as one of the main benefits.

Additionally, the upcoming shift to T+1 in the US, Canada and Mexico in May 2024 poses additional pressure on us to follow the same approach to avoid a potential gap in the perceived competitiveness of European markets. Other jurisdictions such as India have already made the move. And more importantly, current discussions held in the UK should be followed closely.

This context aside, the unique nature of the European Union infrastructure means important challenges remain to be considered. Multiple trading venues, central counterparties, and central securities depositories, together with several currencies, help create a complex ecosystem with additional frictions. Navigating this fragmentation requires a comprehensive understanding of diverse regulatory frameworks and market infrastructures, adding yet more complexity to the T+1 adoption process.

The impact on the resilience of settlement systems requires a thorough assessment. With less time available to settle trades operational risks may increase. If a shorter settlement cycle is implemented, settlement fails run the risk of increasing which would also lead to a cost increase due to cash penalties.

It should also be mentioned that embracing a shortened settlement cycle would require a high level of automatization and investment costs, with uneven effect on market participants. In this context, smaller players may find it difficult to adapt their systems to a shorter settlement cycle and would require sufficient time to prepare. It is also important to consider to what extent the financial implications of such investments could be passed on to retail clients.

ESMA has already initiated a call for evidence to obtain the perspectives of stakeholders on these matters that will help us to better understand and address any of the risks and challenges before taking the decision to move to T+1. In cooperation with the members of the ESCB, ESMA will prepare a report to guide European authorities on the potential shortening of the settlement cycle.

Regulators should take risks and challenges into account to foster a smooth transition.

Many believe the question is not if, but when and how. In this rapidly evolving environment, European markets can not be caught napping. However, a careful consideration of associated risks and costs needs to be conducted, given that moving to a faster settlement process could also have a negative effect on our attractiveness. A successful transition would also require proper time to allow a smooth compression of the settlement timelines and, more importantly, a joint purpose and coordination of all stakeholders involved.

Europe already has experienced a successful transition from T+3 to T+2 which was the result of planning, testing and coordination across the industry. We are now considering whether to tackle an even more challenging change and it should be done after careful analysis.

PHILIPPE LAURENSY

Managing Director, Head of Product Strategy & Innovation - Euroclear Group

Driving the next phase of securities markets evolution – A collaborative effort

The drive towards ever greater levels of integration and efficiency in the post-trading ecosystem has rightly been a vital component of the European and global securities markets agenda for many years. Advancements in technology and the shift towards a shorter settlement cycle are driving another major evolution in the world's financial markets.

Transitioning to T+1 settlement

Major markets are now focused on a shorter settlement cycle. This is now a topic that looms large in the policy agenda. The transition to T+1 settlement is soon to become a reality in the United States, Canada and Mexico. This is today's reality for many European players active on the global stage, and their experience in North America will be valuable when the shorter life-cycle is rolled out in Europe.

A compression of the settlement cycle carries the prospect of reducing risks and costs in securities markets, as well as furthering the modernisation of capital markets. While these benefits represent powerful drivers, the challenges should not be underestimated. These are not so impacting on the market infrastructure themselves, which can and do handle same-day, real-time settlement. But for dealers, custodians and their clients, shifting to T+1 settlement cycle will require major investments and a collective, coordinated effort among authorities and market participants, underpinned by international collaboration and shared learning.

In the case of the EU, the challenges are compounded by the unique complexities of the single market, involving multiple jurisdictions, settlement locations, stock exchanges, currencies and distinct legal frameworks. The EU therefore needs to carefully consider its next steps and the potential roadmap, taking all asset classes into consideration.

We should also not lose sight of the needs of the end-users of our capital markets – issuers and investors, including the requirements of cross-border investors from outside the region. Assuming the successful migration of North American markets to T+1 this year, harmonising settlement cycles across developed markets will become a compelling driver for EU markets to follow. Regional synchronisation is another major consideration. The EU and the UK should align as much as possible their approaches to T+1 to maintain well-functioning markets. Already desynchronisation of settlement cycles between North America and Europe is creating hurdles for asset managers and ETF providers as well as FX challenges.

> **We are in an exciting phase of market development where FMIs will need to play a central role.**

Finally, shortening the life cycle will definitively increase funding challenges and dependency on efficient secured financing transaction markets including repo and securities lending. Europe will especially look to learn from the US experience in this sector of the market.

Advancing the digital transformation

The rise of DLT, AI and other technologies has the potential to transform the ways in which financial market participants issue, invest and process different asset classes.

In the specific case of DLT and digital assets, we have seen a growing number of initiatives drive a new maturity in the use of this technology, including our own initiative on Digital Securities Issuance end of last year.

Whilst we remain in the early stages of adoption of these technologies, there is little doubt about their long-term potential to support liquidity and deliver benefits at every step of the trade lifecycle, including in relation to settlement acceleration and efficiency.

The digitalisation journey is a long-term endeavour. Work will need to continue on broader regulatory harmonisation and industry-wide standardisation to build the necessary infrastructures and connectivity across DLT protocols and legacy platforms.

A prospective wide-scale introduction of DLT is subject to a longer-term timeline compared to the near-term efforts to shorten the settlement cycle and enhance efficiency. A full transformation towards a digital ecosystem is not a pre-requisite to achieve the T+1 transition. These two evolutions need to be advanced in parallel, according to their different time horizons.

Supporting strong European markets on the global stage

Much has changed in the European post-trading market since the work of the Giovannini group over 20 years ago. The current juncture represents an opportunity to reflect on what has been achieved and the areas where further progress is needed. The overall competitiveness and efficiency of our financial markets and the needs of end-users, together with financial stability and market resilience objectives, should remain our core guiding principles.

Financial market infrastructures and the CSD community, including Euroclear's entities, have been supporting the evolution of financial markets for decades, providing scalable, resilient and trusted infrastructure on which the industry can build. We are in an exciting phase of market development where FMIs will need to continue to play a central role in collaboration with all market players.

JESÚS BENITO
Head of Domestic Custody & TR Operations - SIX Group & Chief Executive Officer - Iberclear

T+1 and beyond: a look into the future of securities settlement

So, it is almost here. The US move to the T+1. The decision which caused an international debate in the capital markets around the world, or at least here in Europe. It has been one of the highly debated topics for the past few months. Yet, it still needs to be analysed in a far more greater detail. By the end of May 2024, we will finally see how this move in the US, Canada and Mexico will affect our markets and the wider industry in reality. Europe should take a careful look at the potential lessons to be learnt, even though the American ecosystems are very different from ours.

The logic says, if it can be done faster and better, why not? Thanks to the highly advanced digital technologies, we are living in an unprecedented world, where speed of delivery of services and products accelerated to a level where the customers expect the instant gratification. Technology gets faster, and the patience grows thinner. It will become even more so in all aspects of our lives facilitated by new technologies and demanded by new generation of digital natives. The post-trade industry will not be an exception.

The new technologies that facilitate T+1 settlement are the GenAI, data, robotics, cloud, automation and APIs, among others. Distributed ledger technology ('DLT'), however, is a totally different ball game. DLT allows the so-called atomic settlement, which is a gross settlement at the very moment when trading is being executed. From this perspective, the atomic settlement not only reduces the settlement cycle, but also it actually eliminates the very concept of the 'settlement cycle' itself, as there will be no gap between trade execution and its settlement. Thus, atomic settlement means a brand new ecosystem. Therefore, it is necessary to distinguish the T+0 settlement cycle in the current legacy system from the atomic one in the DLT ecosystem. With the current technology, a move to T+1 is rather feasible, which cannot be said about the T+0. Therefore, from my point of view, any further shortening from T+1 cycle should be based on a new technology, completely replacing the current legacy systems by a DLT based one.

As many industry representatives have highlighted, there are both advantages and disadvantages to further shortening of the settlement cycle. Detailed cost and benefit analysis, instead of 'copy and paste', should be performed by all stakeholders in order to decide when and how the EU should move to T+1. ESMA's public consultation is the right move in this direction. When EU decides to do so, it would be optimal to do it in a harmonized way together with the UK and Switzerland.

The logic says, if it can be done faster and better, why not?

The path towards achieving T+1 is undoubtedly fraught with challenges. From time pressure and settlement complexities in FX markets for funding cross-border transactions, ETFs difficulties to settle on due date, which is difficult even in the T+2 environment, to navigating corporate events' relevant dates and securities lending, possible surge in operational risks and administrative costs, heavy upfront investment in technology and automation, all to be added to the 'Challenges' list.

However, if there is one issue that worries regulators in Europe above all others, it is the potential increase of settlement fails from the current level, something that would be considered totally unacceptable in some markets.

All these considerations and decisions fall on the shoulders of the next political cycle of the EU, which will commence in the second half of the 2024. Aside from the shortening of the settlement cycle, in my opinion, there are three main topics that should be included in the post-trade agenda of the incoming EU institutions.

First, increasing the efficiency of post trade processes. In order to do so, the EU should further harmonize and increase cross-border transactions through the financial market infrastructures ('FMIs'), increase the EU competitiveness at the global level, enhance the regulations and tax regimes, and decrease bureaucracy. The shortening of the settlement cycle would fall under this priority, together with the improvement of settlement efficiency.

Second, application of the new technologies to the post trade services. This could be done through, but not limited to, the transition from the legacy systems to the DLT systems, tokenization, crypto assets, wCBDC, developing the AI possibilities, deploying robotics and automatization along the value chain, and extending the cloud solutions.

Lastly, the ESG. To realize our sustainability and ESG objectives, in addition to what we need to do internally, we must foster green listings, assist issuers in their green issuances, devise strategies to prevent greenwashing and promote shareholder identification, their active participation, and engagement in shareholder meetings.

Accomplishing these goals and priorities during the upcoming political cycle would not only facilitate a seamless transition to T+1 but also bring the EU one step closer to the completion of the Capital Markets Union.

VALENTINO WOTTON
Managing Director and General Manager of Institutional Trade Processing - The Depository Trust & Clearing Corporation (DTCC)

Strategies for accelerated settlement in the UK and EU

As the US inches closer to its implementation of a T+1 settlement cycle on May 28, 2024, the UK and EU are also exploring the case for accelerating settlement cycles in their markets to achieve greater industry harmonization and other benefits including reduced risk, lowered clearing fund requirements, operational efficiency and improved capital and liquidity utilization.

It is important to note that a successful transition to a T+1 settlement cycle in the UK and EU will require an increase to the current levels of post-trade automation. The Association for Financial Markets in Europe (AFME) published a whitepaper in Q4 2023 that highlighted pain points in current securities processing in the region, such as data quality issues and counterparty behaviors that affect the ability to match and allocate trades, and recommendations on how these obstacles could be removed. T+1 therefore provides an opportunity to enhance operational efficiencies by encouraging market participants to automate manual processes and adopt industry standards and best practices.

Automating post trade processes

Specifically, trade matching is a critical part of the post-trade lifecycle and serves as the first safety check after execution has taken place. When the buyer and seller agree on all the details of their transaction, a trade match occurs, and the settlement process begins. Most importantly, trade matching allows counterparties to identify exceptions that may cause the transaction to fail. The sooner firms can move to settlement and address trade fails, the better the chances of meeting an accelerated settlement timeline. In support of this, we recommend that the UK and EU markets consider mandating that trade confirmation, allocation and matching take place on trade date, allowing for T+1 settlement.

Standing settlement instructions (SSIs) are another critical component of the post-trade lifecycle, as they play a key role in preventing trade fails. Manual SSIs and the absence of storing and sharing SSI data in a standard and automated fashion across the industry introduces risks and inefficiencies into the post-trade process. In fact, it has been observed that inaccurate or incomplete SSIs are often a primary reason for trade failures. Accurate, automated SSIs are key to the facilitation of accelerated settlement.

> **Post-trade automation and standardization can increase settlement efficiency, paving the way for T+1.**

To address both areas - trade matching and SSIs - firms should evaluate best practice solutions that automate and improve post-trade processes. Today, automated central matching platforms enriched with golden source SSI data and workflows that facilitate accelerated settlement already exist and are key to achieving greater settlement efficiency.

According to DTCC's internal data most transactions leveraging an automated central matching platform are matched and agreed on execution date. On average, over 90% of all EMEA cash securities transactions that utilize automation are fully allocated and matched on execution date. At the same time, leveraging a central SSI repository can provide increased transparency and automation while significantly reducing trade failure. This is because all respective market participants seed the SSI data, access the SSI data and enrich the data from a single source, in an automated fashion.

The need for standardization

In addition to the automation opportunities, the lack of standardization in post-trade processing should also be an area of focus in the UK and EU. Currently, there is no uniform identification reference added to transactions that persists throughout a transaction lifecycle. Securities markets should look to how derivatives markets solved this problem with the introduction of Unique Transaction Identifiers (UTIs) for trade reporting purposes. The UTI allows transaction identification to happen near instantaneously and creates greater visibility across the transaction chain. This enables quicker identification and resolution of bottlenecks or settlement lifecycle issues, while reducing operational risks and costs arising from potential settlement fails. The introduction and increased use of standards, such as the UTI, supports the facilitation of accelerated settlement cycles globally.

Understandably, settlement inefficiencies and risk receive a significant amount of attention from financial market infrastructures and regulators. Considering current levels of interest rates globally, the cost of settlement failure has also increased and has a significant impact on client processing from a risk, funding and even balance sheet perspective.

Introducing greater levels of post-trade automation and standardization can increase settlement efficiency, paving the way for accelerated settlement and reduced risk across the region while modernizing and advancing the industry's capabilities. There is no better time than today to advance these conversations.

HAROUN BOUCHETA
Head of Public Affairs and Chief of Staff for Company Engagement & General Secretary, Securities Services - BNP Paribas

T+1: does the EU really have to follow the US?

There is a clear trend at global level to accelerate settlement cycles for cash instruments from the global standard of two business days following the trade date (T+2) to one business day following trade date (T+1).

For jurisdictions where the move to T+1 is already mandated, like the US, the industry should support such a move to actively contribute to local systemic improvements, increased levels of automation and straight through processing.

Having said that, it is a fact that in some jurisdictions the overall environment notably with regards to the market structure could justify that such a move should be carefully assessed. In the EU, the move would imply not only operational and legal challenges but also significant costs and concerns on settlement efficiency.

The fact that ESMA is currently assessing the costs and benefits of a potential shorter settlement cycle in the EU is a good way to move forward but is also an opportunity for the industry to reflect upon the following points.

1. Should we simply move to T+0 settlement?

A move to T+0 - either on an end of business day basis or atomic - would require a much more fundamental change than moving to T+1. The legacy infrastructures and technologies would indeed probably not support such an extensive overhaul and therefore it would imply to be able to reshuffle the whole environment to suit a T+0 settlement.

In addition to this significant technological challenge, legitimate questions could be raised as to whether a move to atomic settlement is desirable. It could imply limited possibilities of netting and the need to prefund each individual trade and result in prohibitively high liquidity and funding costs, negatively impacting the economics of the securities industry.

2. Is a shorter settlement cycle in the EU a competitiveness issue?

Cross-border transactions and international investors are directly impacted when settlement cycles are reduced to only one day as all post-trade processes need to be completed in limited operating hours with the additional constraints of different time zones. Among the main impacts, FX transactions, stock loan returns, corporate actions, global products with components from markets moving to T+1 (ETFs and depositary receipts) as well as time to get executed trades allocated/confirmed/affirmed/instructed are some of the biggest challenges. In addition, the choices made by the EU for a better settlement efficiency through a settlement discipline regime need to be part of the equation.

We should avoid the situation where a rush to move to T+1 ultimately hurts EU firms and EU markets.

There can be large differences in the volumes of cross-border transactions into different markets. In the case of the US, which is by far the most impacting market for Europe, the US Treasury shows that 19.6% of all securities and 16% of equities are held by investors outside the US (roughly half of these 16% are held in Europe). The UK is also a very important market for Europe given the close links between both markets.

The US move to T+1 is expected on 28 May 2024 and the UK is also currently assessing the opportunity of shortening its settlement cycle. Does it justify that the EU speeds up the process and decides to move to T+1 having in mind competitiveness concerns?

The EU should not rush any recommendation to move to T+1 and should take the time to evaluate in detail the ratio of benefits versus costs, and in particular in terms of attractiveness and competitiveness for market participants, local and international investors, and the EU itself, while scrutinizing the US move and any development happening in the UK.

We should avoid the situation where a rush to move to T+1 may result in a massive misallocation of EU resources (human and capital) that could ultimately hurt EU firms and EU markets given the magnitude and costs of the project. In other words, moving to T+1 would not contribute per se to the competitiveness of the EU and to the CMU nor would it give any competitive edge to EU financial markets and EU players.

3. What should be the next steps?

From a cross-border perspective, my view is that in addition to material implementation costs, any rush to move to T+1 in the EU or in the UK may result in exacerbated settlement market inefficiencies (more fails) coupled with a potential loss of liquidity. This risk is increased by the market fragmentation in Europe.

The EU needs to wait for the ESMA report on the costs and benefits. Also, the specificities of the EU should be considered such as its complexity and fragmentation and the associated costs for EU firms of any project to shorten the settlement cycle. This report should also incorporate elements from the US post-implementation and see what lessons can be learnt.

In addition, coordination between jurisdictions and especially within the same region should be encouraged to reduce any impact on operational processes and market liquidity. In other words, we need a truly open dialogue not only between the EU and the UK but also between the EU and jurisdictions where T+1 is mandated.