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CCP supervision in challenging times

Keynote speech

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It is a pleasure to be back after yet another challenging year.

When I last spoke here in this setting, we were trying to understand the fallout from the invasion of Ukraine, in particular the impact on energy products and other soft commodities. We were also seeing increasing concerns regarding inflation. The situation was extremely volatile as we saw severe events emerging such as the halt in nickel trading at LME.

Unfortunately, the events last week in the US and in Switzerland show us how volatile the situation remains. We are still facing a very challenging outlook, with continued pressures on energy markets and, more generally, across financial markets, as investors grapple with the effects of monetary policy changes to their investment strategies and own fund requirements.

Over the past year, ESMA has continuously shown to be agile. For instance, we set up enhanced monitoring systems for stressed CCPs or proposed emergency changes to the RTS on collateral requirements to allow for more flexibility to NFCs which were drafted and enacted in less than a month – which must be some kind of record in the EU.

Another example is the MCM, the market correction mechanism. Within a month of the decision by energy ministers to impose a price cap on TTF futures (and I do not wish to dwell on the mechanism as such, ESMA has provided its views in this regard publicly), we have prepared a comprehensive assessment on the expected impact of the MCM on CCPs and the clearing ecosystem. [While at this point in time ESMA did not identify immediate noticeable effects, we expect market participants to anticipate its application if prices move closer towards the bidding limits.]

While ESMA demonstrated its ability to react under strong market pressures, the past year and also the last weeks have put a spotlight on weaknesses and dark spots in certain areas of our regulatory and supervisory system.

This calls for expanding the strength of the supervised ‘core financial system’ vertically down the client clearing chain, but also horizontally to markets which had until now had gathered less regulatory interest such as commodities, but also crypto products.

The EMIR Review discussions, which have just started, are potentially an opportunity to address these. Let me focus on some key areas in this regard:

1. Down the clearing chain

The COVID crisis had already highlighted concerns as regards to the potential procyclical behaviour of CCP margin models and the preparedness of clearing participants to face big margin changes.

As you may be aware, ESMA launched last year a consultation to look into the existing anti-procyclicality tools under EMIR. After conducting additional analysis to ensure that our considerations are still adequate following the recent energy market crisis, we hope to be able to finalise our considerations before the summer.

However, the procyclicality of certain CCP margin models is only one part of the problem, as clearing members exposed to margin calls will in turn require additional margin from their clients, further adding to liquidity strains on the wider clearing ecosystem.

The extent of such calls may not be too transparent. CCPs are already required to offer initial margin simulations tools to their direct members following EMIR REFIT. The Commission's EMIR 3 package proposes that this information should be passed on by clearing members to their clients, which may have fewer available liquid resources and therefore need to be able to better anticipate large margin calls.

The global standard-setting bodies are conducting work on margin responsiveness and transparency to cater for considerations around APC metrics and margin simulation tools. ESMA is committed to see this work to completion by the end of the year.

In this context, the EMIR 3 discussions may be a good opportunity to ensure that ESMA has the power to consistently implement the conclusions of the international workstreams to ensure that the information provided by both CCPs and clearing members on the margins collected is sufficiently transparent, granular and comparable.

2. Across the field of commodities

The Commission has also made proposals in EMIR 3 to address certain specificities in the field of commodities, in particular the direct participation of NFCs to CCPs.

We consider that the Commission has suggested a balanced approach concerning the margin requirements and default fund contributions to be direct clearing members, including in stressed market conditions, and the prohibition to offer client clearing services.

We welcome the proposed mandate for ESMA to further define what is expected in terms of admission criteria and ongoing membership requirements, in order to consistently strengthen the resilience of clearing members regardless of the type of counterparties.

In its EMIR 3 proposal, the Commission also clarifies that CCPs which offer clearing in both financial instruments and non-financial contracts should be subject to EMIR requirements in their entirety. Similar activities carry similar risks and should be subject to similar rules, therefore CCP requirements should be extended to all non-financial contracts, such as forwards on certain commodities or novel asset classes such as crypto, regardless of whether a CCP also clears financial instruments.

Finally, the Commission has also suggested improvements on reporting requirements. Throughout the energy crisis in March and August last year, EU and national authorities were not able to identify comprehensively the exposures across clearing members, clients, but also of subsidiaries of a group based in a Member State different from the one where the trading arm is based.

The MCM Regulation put reporting issues further in the spotlight. While Council required that ESMA regularly monitor and assess the potential impact of the MCM on CCPs, ESMA had to rely on voluntary data submitted by EU CCPs transmitted by NCAs, as EMIR reporting only covers transaction data and not information on the CCP's risk management. We need to enhance reporting by EU CCPs, to enable a comprehensive, consistent and EU wide monitoring and assessment of potential systemic risk.

3. Under supervision

As you may expect, I cannot do a keynote speech without a few words on the improvements proposed by the Commission in respect to the EU CCP supervisory system.

I fully agree with the Commission that the introduction of clear and efficient supervisory processes is essential to ensure a fast time-to-market so that EU CCPs are able to compete globally. We still see CCPs waiting months, if not a year, for NCAs to declare completeness on their application. We believe that the Commission's proposals to introduce maximum deadlines and to run processes through NCAs, ESMA and the colleges in parallel will help win valuable time.

Moreover, the proposed procedure for non-objection, which aims to simplify the approval process for non-material or non-significant changes in the CCP, is also welcome – as long as there is a clear definition of non-material extensions of services or non-significant changes to risk models, as this would otherwise increase supervisory divergence across NCAs.

And I do not say this lightly: supervisory divergence across NCAs remains a critical issue in the EU. The same issues are coming up time after time. Some CCPs benefit from 'catch-all' authorisations, some CCPs are allowed to outsource certain activities without NCA approval, or the EMIR compliance of CCPs is still assessed in very different ways across Member States.

The Commission's proposals in these matters are vital, expanding the scope of the CCP Supervisory Committee's work and strengthening the tools for supervisory convergence, in particular the requirement on NCAs to justify deviations from agreed supervisory approaches.

Last but not least, the proposal to increase the role of ESMA in colleges would go a long way towards enhancing consistency, as ESMA is the only authority participating across all colleges. While some of these measures may be controversial, they would be essential steps towards strengthened consistent supervision for the EU CCPs, in particular if, as a result of the measures to reduce exposure levels to UK CCPs, they will have to manage higher levels of systemic risks.

However, there are also areas which have not been sufficiently addressed in the Commission proposal. Additional ESMA powers would be warranted to address crisis situations and to cater for CCP recovery and resolution of Tier 2 CCPs. It may also be worthwhile reviewing the current comparable compliance regime, in particular to the extent that Tier 2 CCPs are still of substantial systemic importance.

4. Crossing the sea

Let me conclude with taking a look at the global dimension of CCPs and the need for regulatory cooperation. Cross-border cooperation requires high levels of trust, transparency and coordination among partner jurisdictions. The need for sharing of information and cooperation on matters of legitimate interest also exists with non-EU jurisdictions, in particular where exposures for European participants and markets are high. ESMA stands ready to work on the basis of global best practice such as cooperation arrangements which improve exchange of information to better identify emerging risks and coordinate adequate responses, while allowing for appropriate deference.

Over the past years, we have developed a robust relationship with the Bank of England and believe we can further deepen this cooperation in particular in the field of crisis management. We have also engaged with a high number of other supervisors in the context of third-country recognitions. Of course, current geopolitics do not help, but we are still proud to say that ESMA has concluded 25 EMIR compliant MoUs with authorities all over the globe – including brand new ones with Chile, China, Colombia, Israel, Malaysia and Taiwan – covering 39 TC-CCPs currently recognised by ESMA.

Where there are common interests, there is a way for cooperation: and we glad to see that trust and cooperation is the way chosen by the vast majority of supervisors across the globe.