PENSION FUND PERSPECTIVE
-- Impact of regulation on derivatives markets and risk absorption --
Introduction

- Declining liquidity in instruments where banks make markets
- Causes large swings in markets
- Crowded positioning of market participants contributes to this problem
- Pension funds and asset managers should realize that changing their asset exposures costs either more time or money
Lower liquidity causes larger collateral swings

Source: APG – daily cash collateral flows
Regulation impacts markets, but at important reporting dates the impact is very pronounced.

Source: APG – Implied US rate based on FX forward prices and Eur-cash market rates
Conclusion based on our observations: Regulation and Market Trends are causing significant changes in markets and market structure

- Market liquidity is declining and will continue to decline – bifurcation of financial markets
- Trading costs will go up
- Funding costs for companies in real economy will rise
- Market liquidity will evaporate quickly in stress scenarios
- New firms are active in FI market making (Citadel Securities)

**EMIR**
Clearing obligation, transaction reporting requirements.

**CRD IV**
Banking Capital Requirements

**MiFID 2**
Mandatory trading on regulated venues, best execution requirements, transparency requirements.

- Shift to cleared products
- Reduced Liquidity
- Segmented Markets
- Electronification
- Transparency
Discussion items

1. Do BMCG members recognize the “report date stress” in markets and is this a cause for worry?

2. Does regulation create risks by:
   - pushing the market towards cash-only collateral for both cleared and non-cleared derivatives?
   - at the same time increasing illiquidity in FX forwards, cash- and repo markets?