Practical Implications of T+1 for Buy-Side e-FX Traders

Foreign Exchange Contact Group ECB Frankfurt am Main, 16 November 2023
What elements of their existing e-FX trading processes should Buy-Side Traders review, to ensure readiness for T+1?

1. Operational Risks - Are counterparties, vendors, custodians and settlement and clearing service providers adequately prepared to support T+1 e-FX trading?

2. e-FX-Trading Setup – Are existing “onboarding” processes fast enough to enable clients to trade T+1 related FX on new accounts without taking on additional T+1 settlement risk?

3. Pre-Trade Netting of FX Orders - Are changes needed to existing pre-trade netting processes?

4. Bulk Transactions - Are changes needed to mitigate settlement risk?
   a) Transact a series of “sweep trades” through the day to clear most FX exposures more quickly.
   b) Process one bulk FX trade on T+1, then a “true up” trade on T+0.
   c) Pre-Fund FX for T+1 transactions.

5. Program Trading - Do program trades need to be completed earlier in the day to ensure T+1 settlement?
What elements of their existing e-FX trading processes should Buy-Side Traders review, to ensure readiness for T+1?

1. WM / BFIX Benchmark Trades - Are any changes needed in terms of timing and processing of fixing orders?

2. FX Rollovers - Does the rollover of FX positions have to be carried out earlier (i.e. so that any P&L can be reinvested in the underlying securities on the same day)?

3. Post Trade Allocations (PTA) - Are changes needed to the PTA process (i.e. to split up T+1 vs T+2 transactions or to PTA trades based on counterparty / custodian capabilities)?

4. Cancellation and Correction - Are post trade correction and cancellation processes through existing e-FX trading venues and internal Order Management Systems robust enough to mitigate potential T+1 settlement issues?

5. Documentation – Does documentation require updating (internal / external) to describe changes to e-FX trading processes that must be adopted in readiness for T+1?
T+1 SETTLEMENT

November 2023

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FX EXECUTION & SETTLEMENT TIMELINE

**Equity Trade Date**

- Trade Date $T$
  - $T - 22:00$ CET / $16:00$ ET

**Equity Settlement Date**

- Start of CLS Settlement
  - $T+1 - 00:00$ CET
  - $T+1 - 7:00$ CET
  - $13:00$ CET

- GBP and EUR Settlement cut-off
  - Clients should execute ON transactions before 15:40 CET (depending on custodian cut-off)

- FX Liquidity Peak
  - Asia, Europe and US are active at the same time

Big part of the volumes is executed just before US cut-off

“witching hour” very scarce FX liquidity

Initial pay-in schedule issued

US equity trade execution
- Reconciliation
- Confirmation
- Matching

CLS Cut-Off

In/out swap process
**FX HEDGING ALTERNATIVES**

1. Execute T+1 FX deals early enough to settle in CLS
   - Depending on the execution time, investors may see an increase in costs
   - Investors may consider the possibility to have an operational set-up in the U.S.

2. Execute T+1 (after CLS Cut off would ) or T+0 FX deals
   - Increase of Settlement risk
   - Potential impact on the Delivery limit usage on banks and clients' side

3. Prefund the security transactions: Investors keep executing FX during the best liquidity hours then adjust any discrepancy
   - Investors could externalise their FX need to their custodian to reduce their settlement risk
TALKING POINTS

**FX Liquidity**
- Could we see FX liquidity improvement during NY afternoon?
- Could the FX spot convention switch to T+1? (on MDPs, Order books...)

**Streaming**
- Would AM continue to use WMR 4PM fixing orders?
- WMR 1PM?

**Documentation**
- Some institutions consider T+1 and T+0 as derivatives that need ISDA and CVaR/RDL. Investors could have smaller liquidity pool?

**Pre-Funding Securities**
- Will prefunding add operational complexity? Additional costs?

**Banks Funding**
- Trades executed close to CLS cut off may be challenging to hedge, could they trigger intraday limits? USD funding?

**EU Securities**
- Should Europe profit from the lessons learnt on the US securities moves before extending the change to EU securities?
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