

Made-Available-to-Trade (MAT): Evidence of Further Market Fragmentation

April 2014

Summary

On May 16, 2013, the Commodity Futures Trading Commission (CFTC) approved the ‘made-available-to-trade’ (MAT) rule, which gives the market clarity on which products must be, by law, traded on swap execution facilities (SEFs). Once the CFTC issues a MAT determination, a mandate is established for trading that product on SEF, which prevents it from being traded bilaterally by counterparties subject to the SEF requirements.

This analysis builds on ISDA’s earlier work on SEFs by focusing on the effects of the MAT regulation and its potential impact on market fragmentation.¹ By using Depository Trust & Clearing Corporation (DTCC) publicly reported data, we approximate the portion of SEF trading comprised of MAT swaps, and track changes to volume measured as gross notional and daily trade count since the start of the SEF regime on October 2, 2013 – and, in particular, since the first MAT determination came into force in February 2014.²

Our findings reveal:

- MAT swap volume accounted for 70% of total SEF trading in interest rate derivatives in the week ending March 28, 2014 (Chart 1)
- During this period, USD MAT swaps comprise 91% of total MAT trading; EUR and GBP MAT swaps account for only 6% and 3%, respectively (Chart 2)
- Following the February 15, 2014 implementation date for the first MAT determinations, SEFs likely became more US-centric, with USD MAT volume increasing and EUR MAT volume declining sharply (Chart 3)
- A comparison of EUR MAT swaps before and after the rule came into effect reveals the average daily notional traded on SEFs declined by 30%, while the average daily trade count fell by 11% (Table 1)
- The MAT rule appears to have created smaller, less liquid pools for EUR and GBP swaps on SEFs relative to USD swaps (Chart 4), and has reduced the dispersion of daily trade size for all MAT swaps (Chart 5)

¹ See *Cross-Border Fragmentation of Global OTC Derivatives: An Empirical Analysis, 2014, ISDA* and *Footnote 88 and Market Fragmentation: An ISDA Survey, 2013, ISDA*

² The data used in this analysis reflects swaps made available to trade (MAT) as of February 18, 2014. MAT submissions are available on the CFTC website: www.cftc.gov

Introduction In a January 2014 report (*Cross Border Fragmentation of Global OTC Derivatives: An Empirical Analysis*), ISDA studied the possible effects of uncoordinated national legislation and regulations. Findings revealed that changes in trading behavior had occurred between European and US dealers once the SEF regime had come into force on October 2, 2013. European dealers began to trade exclusively with other European counterparties in the market for EUR interest rate swaps and had dramatically moved away from trading with US counterparties. The resulting market fragmentation created separate liquidity pools for US and non-US persons.

SEF volume represented about 51% of total rates trading reported to the DTCC SDR for the week ending March 28, 2014. This activity is largely US-centric. Trading of EUR swaps on SEFs has declined significantly since the first MAT determinations were implemented in February 2014.

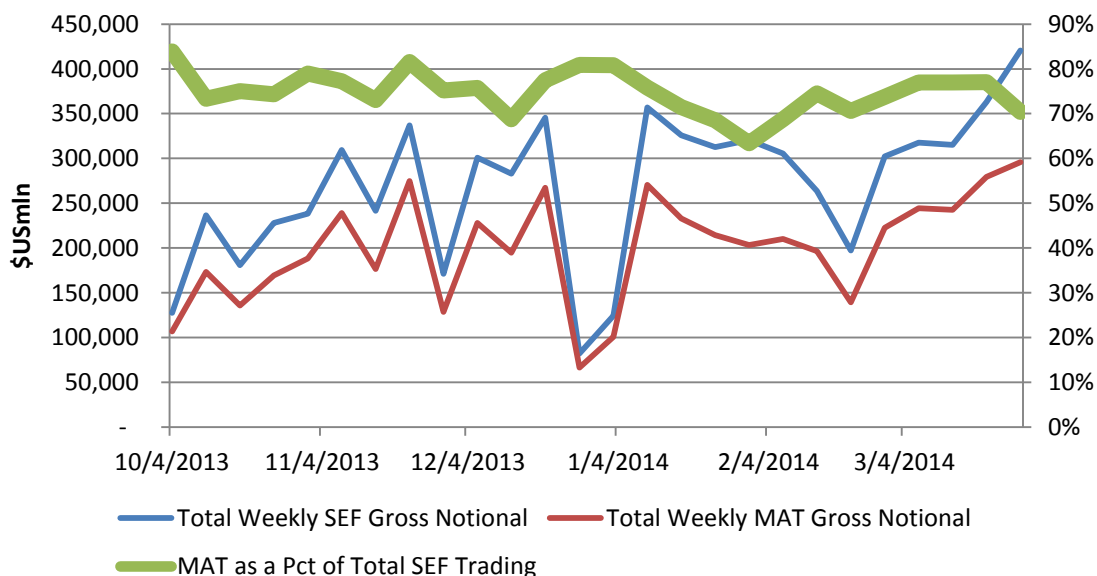
This appears to substantiate findings of an earlier ISDA survey in October 2013 (*Footnote 88 and Market Fragmentation: An ISDA Survey*), which reported that 84% of survey participants believed non-US persons were choosing not to trade on a SEF. Participants predicted this shift away from SEFs would be exacerbated once swaps were made available to trade. This important dynamic is the focus of this analysis, as MAT swaps must trade on a SEF and are no longer permitted to be transacted bilaterally.

MAT Swap Statistics At the time of writing, several types of USD, EUR and GBP interest rate swaps had been approved by the CFTC for MAT trading. These include spot and forward-starting USD swaps with three- or six-month Libor floating rate references, as well as spot-starting EUR and GBP swaps referencing three- and six-month Euribor and GBP Libor, respectively. Various tenors of one to 30 years are included for all three currencies.³

MAT swap trading volume, measured in terms of gross notional, accounted for 70% of SEF trading in the week ending on March 28, 2014, as shown in Chart 1. In this period, USD fixed- floating MAT swaps account for over 91% of total MAT volume, as well as 64% of SEF trading volume.

³ DTCC data is reported in various formats. Given the nature of these formats this analysis makes several qualifying assumptions regarding what qualifies as an MAT swap. Please refer to the MAT swap methodology section for further details.

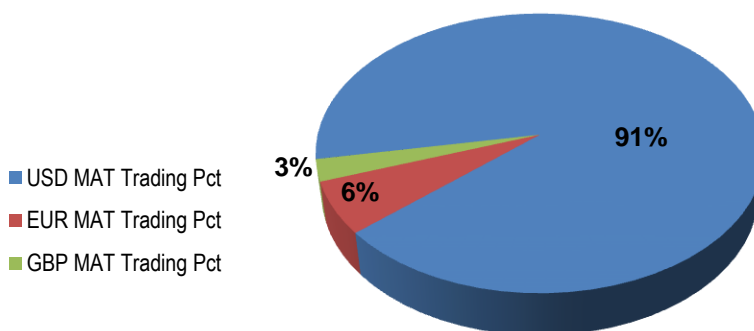
Chart 1: Weekly MAT swap gross notional as a percentage of total SEF volume as of March 28, 2014



Source: DTCC data repository

Chart 2 summarizes MAT swaps by currency as a percentage of total MAT trading. EUR and GBP MAT swaps volume contribute only 8% to total MAT trading volume measured by gross notional. This is not surprising as fewer types of EUR and GBP swaps have been approved for MAT trading by the CFTC, and SEFs continue to provide mostly US-centric liquidity.

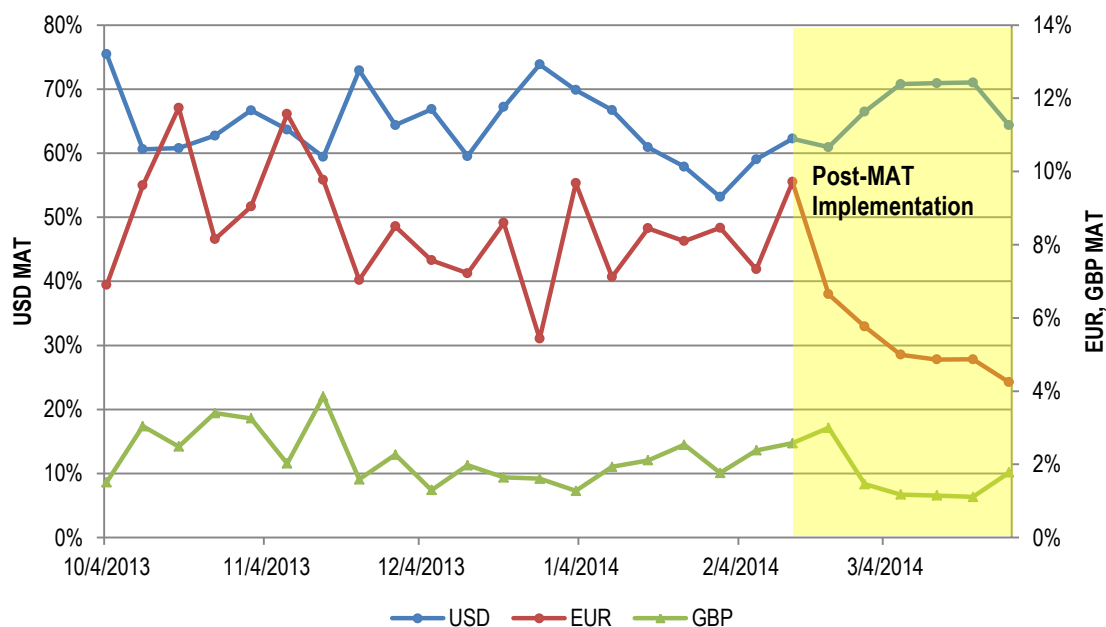
Chart 2: Weekly MAT swap gross notional as a percentage of total MAT volume by currency as of March 28, 2014



Swaps with MAT determinations are no longer able to be traded bilaterally and must trade on a SEF by counterparties subject to the SEF requirements. In order to understand the effects of further market fragmentation resulting from the February 15, 2014 MAT implementation date, we observe weekly MAT swap statistics as a percentage of total SEF trading in Chart 3 below.

There are several interesting trends following the MAT implementation date, which suggest markets are further fragmenting. Most notably, we observe a sharp decline in EUR MAT swaps (red line) as a percentage of total SEF trading volume following the week ending February 14, 2014. We also see a lagged modest decline in GBP MAT swaps (green line) following the week ending February 21, 2014. As a result, USD MAT swaps (blue line) as a percentage of total SEF trading volume increase as SEF liquidity continues to become even more US-focused.

**Chart 3: MAT swaps as a percentage of total SEF volume
as of March 28, 2014**



The character of swaps that are now approved for MAT trading has also changed. A comparison of data before and after the February 15, 2014 MAT rule date reveals that USD MAT average daily gross notional and trade counts have increased 29% and 36%, respectively. These metrics have decreased significantly for EUR MAT trades. EUR average daily gross notional and trade counts have decreased 30% and 11%, respectively. The average daily EUR MAT trade size shrunk 21% as the market becomes less liquid. GBP MAT trades show a similar, but more subdued, pattern when compared to EUR MAT. Average daily notional, trade size and trade count statistics of MAT swaps are presented in Table 1.

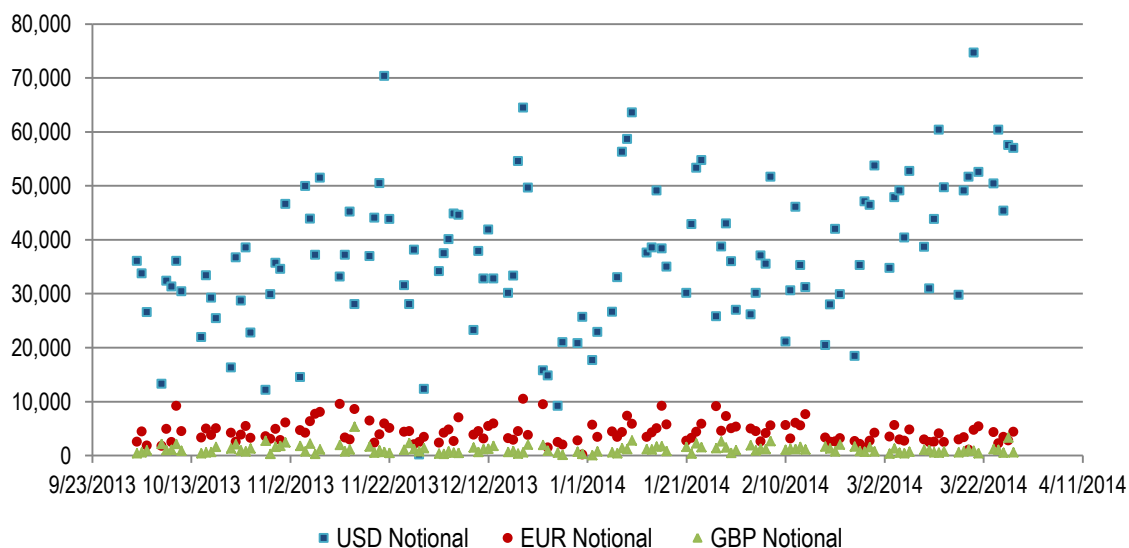
**Table 1: Comparison of daily MAT volume metrics by currency
(October 2, 2013 – February 14, 2014 versus February 17, 2014 – March 28, 2014)**

MAT Swap	Avg Daily Total Notional	Avg Daily Trade Size	Avg Daily Trade Count
Change in Average Values			
USD	29%	-5%	36%
EUR	-30%	-21%	-11%
GBP	-19%	5%	-16%
Change in Median Values			
USD	36%	-6%	38%
EUR	-33%	-20%	-5%
GBP	-32%	-2%	-34%

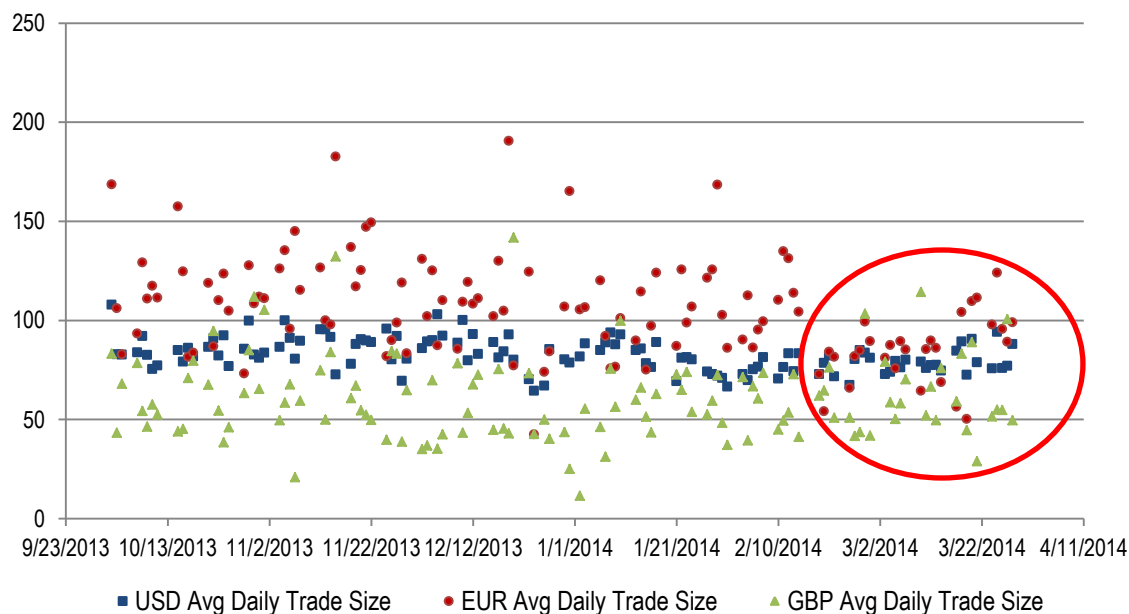
**Market
Fragmentation:
SEFs
becoming
more
US-centric**

The MAT rule appears to have created smaller, less liquid pools for EUR and GBP swaps relative to USD swaps. Chart 4 highlights the large differences in daily MAT gross notionals in USD, EUR and GBP trading. Interestingly, the rule has also reduced the dispersion of the average daily trade size of all three currencies as highlighted in Chart 5.

**Chart 4: Total daily MAT gross notional by currency (\$USmIn)
(October 2, 2013 – March 28, 2014)**



**Chart 5: Average daily MAT trade size by currency (\$USmIn)
(October 2, 2013 – March 28, 2014)**



Conclusion The CFTC MAT rule means bilateral trading of certain USD, EUR and GBP swaps is now prohibited by counterparties subject to the SEF requirements. This analysis measures changes in MAT swaps before and after the February 15, 2014 effective date. Findings reveal that USD MAT swap volume increased while EUR MAT swap volume sharply decreased as a percentage of total SEF volume. As a result, SEFs are becoming even more USD-centric, offering less liquidity to EUR and GBP MAT trading.

MAT Swap Methodology The DTCC publicly available real-time DDR data was utilized for the purposes of estimating volume and trade count statistics of swaps recently made available to trade. Because of the nature of the data and various reporting formats, this analysis utilized the following criteria in order to determine which swaps qualify as MAT swaps:

1. USD, EUR, and GBP swaps that include payment frequencies, resets and day count conventions matching approved MAT swap criteria
2. USD swaps that are no more than two IMM dates between reported trade date and effective dates
3. USD, EUR, and GBP swaps that mature at terms included in the MAT determination
4. USD, EUR and GBP swaps that trade 'on venue'
5. USD, EUR and GBP swaps that reference a three- or six-month Libor, Euribor or GBP Libor reference (floating leg)

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ISDA's pioneering work in developing the ISDA Master Agreement and a wide range of related documentation materials, and in ensuring the enforceability of their netting and collateral provisions, has helped to significantly reduce credit and legal risk. The Association has been a leader in promoting sound risk management practices and processes, and engages constructively with policymakers and legislators around the world to advance the understanding and treatment of derivatives as a risk management tool.

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ISDA's work in three key areas – reducing counterparty credit risk, increasing transparency, and improving the industry's operational infrastructure – show the strong commitment of the Association toward its primary goals; to build robust, stable financial markets and a strong financial regulatory framework.

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