ISDA Safe, Efficient Markets
Celebrating 40 Years

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Opening Remarks
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Good morning, and welcome to the ISDA Treasury Forum. Thank you to CME Group, our founding sponsor, for partnering with us again on this event, and to our gold sponsors, Clearly Gottlieb and Smart Communications.

As you may be aware, ISDA is celebrating its 40th anniversary this year.

The International Swap Dealers Association, as it was originally known, was established in 1985 with a clear objective. A small group of dealers wanted to alleviate the growing documentation backlog, so they got together to agree a common terminology and develop standard-form agreements.

That was only the start of the ISDA story. Today, our membership spans more than 1,000 entities across 76 countries.

Time and again over the past 40 years, ISDA has developed critical standards and best practices and helped firms navigate seismic industry transitions.

From the introduction of post-crisis regulatory reforms to the removal of LIBOR, ISDA has consistently worked with its members to enable industry changes to be implemented safely and efficiently.

As we look to the future, there's another major industry transition on the horizon.

The US Treasury market is about to undergo profound regulatory reforms to improve its resilience and stability, including mandatory clearing requirements for certain cash and repo transactions.

The Treasury market is the world's deepest and most liquid financial market and is the primary means by which the US government raises funding. Treasury repos are also widely used to support the exchange of collateral, which is central to the functioning of the derivatives market.

With outstanding issuance of nearly $30 trillion, the market is forecast to grow to $52 trillion by the end of 2035.

In short, this is a systemically important market that plays a vital role in the global economy. It's therefore critical that the market functions safely and efficiently and remains liquid and resilient during periods of stress.

Regulators think clearing is part of the answer.

The Securities and Exchange Commission (SEC) finalized its Treasury market reforms in December 2023 and the first clearing mandates for cash transactions are due to come into effect at the end of 2026, with repos following six months later.

As it stands, however, banks will be severely limited in their ability to participate in this market.

Important changes must be made to the regulatory framework to ensure banks have sufficient capacity to offer client clearing and intermediation services, so the US Treasury market remains deep and liquid – in both good times and bad.

In these remarks, I'll set out the changes that must be made to ensure Treasury clearing can work as regulators want it to.

I'll also explore the industry work that is underway to prepare for Treasury clearing.

Regulatory framework

There are three distinct flaws in the US capital framework that would make it very difficult for banks to provide liquidity and support the increase in clearing that sits at the heart of the SEC's US Treasury reforms.

All three flaws must be fixed.

The first is the supplementary leverage ratio (SLR), which acts as a non-risk-sensitive constraint on banks and can hamper balance sheet capacity, particularly during periods of stress.

In April 2020, at the height of the global pandemic, the Federal Reserve temporarily excluded US Treasuries from the SLR calculation. ISDA has proposed reintroducing this exemption on a permanent basis to ensure banks have the capacity to provide intermediation and client clearing services.

Senior policymakers – including Federl Reserve chair Jerome Powell – have acknowledged that the SLR needs to be reformed, and we would urge US banking agencies to conduct a consultation as soon as possible to determine the best way forward.

The second issue is the impact of the proposed Basel III endgame rules and the capital surcharge for US global systemically important banks (G-SIBs).

Analysis by ISDA and SIFMA has shown that these two measures would increase capital for G-SIB client clearing businesses by more than 80%.

This punitive tax is completely at odds with the policy objective to promote greater use of client clearing.

It would challenge the economic viability of client clearing businesses at precisely the time when thousands of firms will be looking to banks to help them clear their US Treasury and repo transactions.

This is a serious calibration error that must be corrected to avoid disproportionate capital increases that would thwart the transition to Treasury clearing.

Finally, it's critical that the amount of margin posted and corresponding bank capital requirements reflect the actual risk in client portfolios.

Clients must be able to realize the benefits of cross-margining and related cross-product netting across US Treasury securities and futures.

Cross-margining programs have been a widely accepted part of cleared markets for two decades. They ensure the initial margin posted reflects the actual risk of a portfolio of trades, even if those trades are cleared at different central counterparties.

For example, the Fixed Income Clearing Corporation (FICC) and CME operate an approved cross-margining program that enables clearing members to realize initial margin efficiencies from offsetting trades in a portfolio of Treasury cash, repo and futures transactions.

It's critical that this cross-margining program is extended to client transactions and regulators act quickly to approve it once they do.

There's also no recognition in the capital framework of the risk-reducing benefits of netting across US Treasury repos and futures.

Without this recognition, banks will face elevated capital requirements because of higher exposures, combined with reduced margin posted by clients under the cross-margining program.

In this scenario, a bank would either be forced to require a customer to post the full amount of margin – foregoing the benefits of cross-margining programs – or face a significant increase in capital requirements.

Let me be absolutely clear. If we're to successfully transition to increased clearing in the US Treasury market, these flaws must be properly addressed.

ISDA has analyzed each issue in detail and proposed potential fixes. Unless these fixes are applied, bank balance sheet capacity will come under strain, threatening the ability of banks to absorb the massive supply of new Treasury issuance and facilitate client clearing. Disruption in the Treasury repo market could also impair the exchange of collateral for cleared and non-cleared derivatives.

The stakes are high and there are no shortcuts.

ISDA will continue to engage with policymakers to make sure the prudential framework is appropriately adjusted so it supports, rather than impairs, liquidity and resilience in the Treasury market.

Industry preparation

Before finishing, I'll briefly highlight the state of play in terms of preparations.

Last year, FICC released proposed changes to its rule book, while CME has published proposals for a new clearing service. ICE has also announced it will launch a Treasury clearing service.

As it stands, FICC offers several varieties of direct clearing and sponsored clearing and has proposed a new agency model. CME's proposal includes direct clearing plus two varieties of agency-like clearing.

These services all entail different obligations for members and users, and would have varying implications for collateral segregation, accounting and netting.

Market participants need to make sure they're up to speed with the different clearing services that will be available – and our first panel this morning on clearing models should help with that.

If you want additional information, ISDA has published a comparison of various clearing models for US Treasury transactions and derivatives, and we'll continue to update this as new models emerge.

We've also been participating in an industry group led by SIFMA that's developing appropriate client documentation.

Good progress has been made, but the documentation needs to work for the various clearing models and rule books that are still being developed, as well as client segregation solutions, some of which have yet to be finalized. Work is also needed to make sure the documentation covers done-away clearing.

Once documentation has been finalized, dealers will need to execute the documents with thousands of counterparties, as well as obtain netting opinions in the US and multiple foreign jurisdictions to ensure efficient capital treatment.

We know from the implementation of margin rules for non-cleared derivatives that this is a considerable amount of work and it will take time.

ISDA will continue to work closely with clearing houses and market participants to make sure momentum is maintained in the months ahead.

Conclusion

I started these remarks by reflecting on ISDA's 40^{th} anniversary and how we never shy away from addressing the biggest challenges confronting financial markets.

From the removal of LIBOR to the rollout of margin requirements for non-cleared derivatives, every challenge was unique, but the process has remained consistent. We analyze the issues, we engage closely with our members and policymakers, and we help to develop solutions when they're needed. And together, we effect change.

Treasury clearing is no different. It's a huge change for the world's most systemically important market, so we must get it right.

With close collaboration between the public and private sectors and diligent preparation, I'm confident we will.

Conferences like these provide a valuable forum for discussion. They help market participants get to grips with the changes that are coming and the challenges that need to be overcome.

I'd like to close by thanking all our speakers, sponsors and delegates, and I hope you find the sessions constructive and engaging.

To get us started, I'd like to introduce Agha Mirza, managing director and global head of rates and OTC products at CME Group, who will give some welcoming remarks.

I'd also like to take this opportunity to thank CME once again for working with us on this event and for being such a great partner.

Agha, over to you.