

Making settlement easy

Derek Duggan - 6 Sep 1999

The arguments for single regional settlement utilities are compelling

The concept of having regional clearing and settlement utilities for securities transaction processing is undeniably attractive if it could be properly constituted. This would be particularly appropriate if local clearing, depositories and payment systems could be linked to provide participants with single window access to each region.

This, however, is not yet a reality. Central securities depositories (CSDs) play an important role in the development and maintenance of domestic capital markets, and increasingly in cross-border investment. CSDs continue to proliferate; rising from 13 in 1980 to 102 operational CSDs and 20 planned across 96 countries today. The design, ownership and structure of CSDs have a major impact on the asset safety of investments held in domestic markets. This has been highlighted by recent regional difficulties, particularly as the strength of many local commercial banks has weakened.

Europe is a good example of regional integration, with the competing initiatives to create a European clearing house. Outside [Euroclear](#) and [Cedel](#), the catalyst driving regional co-operation remains with the local CSDs themselves. Euroclear is launching a new bank and is revisiting its proposed hub and spokes proposal. [Cedel International](#), which combines the German depository, [Deutsche Börse Clearing](#) (DBC) and possibly its French equivalent, [Sicovam](#), as partners, is currently pushing to build a European clearing house. The [European Central Securities Depositories Association](#) (ECSDA) has plans of its own for creating an integrated regional clearing and settlement environment. They are promoting the idea of bilateral links between its members, often known as the 'spaghetti model', due to its diagrammatic image. [Crest](#), a leading member of [ECSDA](#), is a proponent of the regional hub concept, although DBC's decision to link up with Cedel has largely derailed this drive in its original form. It has already announced a bilateral link with SIS, the Swiss depository, which will provide trade settlement in Swiss securities free of payment, although plans are in place to provide delivery versus payment in euros in 2000. With the cash element missing this latter arrangement could magnify custody risks.

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Outside Europe, CSDs are establishing what could be the foundation for future inter-regional co-operation, with the development of existing, and the creation of new, regional associations - including the Asia-Pacific Central Securities Depository Group (ACG) and the Central and Eastern European Central Securities Depositories and Clearing Houses Association (CEECSDA). Preliminary discussions among the North and South American CSDs took place in August with respect to forming a closer working relationship.

The next few years will certainly see many changes among CSDs which should facilitate future co-operation. A number of steps will improve post execution/pre-settlement efficiency. These could include a move towards straight-through processing and a reduction of settlement cycles.

A drive to improve asset safety and risk minimisation of settlement and safekeeping in local markets will become more important. Increased convenience, improved efficiency (including cost-effectiveness) and minimisation of risk will continue to be the drivers of change.

As these issues will almost certainly override national interests in the same way that securities transactions already transcend national borders, new linkages will be created and some CSDs may find it more effective to form alliances and partnerships, and perhaps merge for survival.

The need to formally assess and evaluate CSDs and related risks cannot, however, wait until the possible future creation of any new regional utilities.

Pressures exist today to reduce custody risk exposures, and the investment community is on notice to better understand local market infrastructure, conditions and related risks.

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