acuiti management intelligence

Derivatives Post-trade: From Ancillary to Alpha

IN ASSOCIATION WITH

OSTTRA

Executive foreword

By Erik Petri, Head of Optimisation, OSTTRA

For decades, post-trade operations have been treated as a necessary utility - a cost centre focused purely on managing fragmented post-execution workflows. OSTTRA was established precisely to resolve this systemic operational fragmentation across post-trade derivatives. Today, however, the ground has shifted beneath our feet. The need for connected, resilient infrastructure has never been more urgent. We commissioned this research because the derivatives industry is currently crossing a critical inflection point.

According to our latest industry survey, while a strong 78% of respondents feel their processing systems are robust enough to manage volume spikes caused by geopolitical shocks, a massive nine in 10 now identify post-trade investment as a strategic priority. The question is: why the sudden pivot?

The answer lies in the intense, compounding pressures of modern market structure. The global transition to T+1 settlement is serving as a forcing function. Under this compressed timeline, speed without accuracy - and accuracy without speed - are equally detrimental to a bank's or broker's ability to service their clients. Without the timely trade data to support superior trade messaging, confirmation, and affirmation processes, firms risk costly settlement breaks that immediately bleed into increased regulatory costs and bloated liquidity requirements.

Simultaneously, we are watching a shifting global regulatory landscape. With the US G-SIB framework expected to move toward average daily gross notional figures rather than static end-of-year snapshots for G-SIB ranking and capital add-on, the ripple effects are likely to be felt by European and global banks alike.

These pressures have changed the mandate for post-trade. Our view is that front-office traders should be empowered to focus solely on execution. It is the responsibility of a modernised post-trade infrastructure to absorb the complexities of portfolio and liquidity management on the back end.

When we do this correctly, we unlock genuine capital optimisation - genuine post-trade alpha. High-quality, "golden copy" data allows firms to hedge risk more effectively, leading to tighter bid-ask spreads and superior client service. For example, by implementing "settle-to-market" workflows in OTC derivatives - which drops the margin period of risk to a single day - firms can slash capital requirements by approximately 50%.

The findings in this report map directly to a new strategic trajectory for the sell-side: Accelerate, Optimise, and Differentiate. By establishing accurate, trusted data more quickly (Accelerate), firms unlock balance sheet efficiency (Optimise), which ultimately transforms post-trade from a processing centre into a definitive competitive edge (Differentiate).

The data that follows in this report details exactly why - and how - the industry is making this transition.

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Introduction

Post-trade derivatives operations have moved through a series of exceptional challenges in recent years. From adapting to higher volume and higher volatility conditions, along with more frequent margin calls, fragmented CCP liquidity and increased legal entity complexity after a run of buy-side consolidation, systems' capacity has been heavily stress-tested.

However, the current situation in post-trade is not one of reactivity. As firms invest in their back-office operations, they are also realising that an optimised post-trade infrastructure can unlock significant benefits across their firm. Structure it correctly and post-trade optimisation can provide meaningful capital relief to an organisation.

Infrastructure that takes the complexity of calculating the all-in cost of trading off of a trading desk can also become a significant competitive advantage for the front-office. No longer is post-trade functionality simply a cost centre, for many it is becoming a competitive advantage.

Our latest research has found that this is pushing the sell-side towards a new wave of investment, as firms seek to overcome inefficiencies in their post-trade operations.

Data quality will be essential to this next stage in the evolution of post-trade, both for reducing the classic frictions of processing and for harnessing the full power of AI.

Understanding every element of post-trade infrastructure, from booking models to lineage is becoming a foundational step in generating the high quality and trustworthy data that effective AI models need.

To investigate these themes in depth, Acuiti has partnered with OSTTRA to survey and interview 45 sell-side firms on their approaches and attitudes to post-trade infrastructure. Firms comprised a mix of multinational banks and non-bank FCMS, as well as regional banks and clearing brokers.

The key findings are:

- 96% of firms with OTC derivatives activity and 89% of those participating in listed derivatives markets saw better post-trade netting and optimisation as a significant route to balance sheet and capital efficiency
- 86% of firms see superior post-trade transparency, speed, and automation as a key competitive differentiator when servicing institutional clients, with 43% saying it is already a significant driver of client decisions
- Commissions and fee payments were cited by 64% of respondents as the main pain point caused by poor data quality, while 54% said it impacted T+1 reconciliation and exception management
- 66% of firms said that their listed derivatives operations teams were spending more than 10% of their time resolving post-trade exceptions, fails and settlement breaks
- 82% of firms said that more than 10% of their bilateral OTC derivatives trades were confirmed manually rather than electronically

Pain points

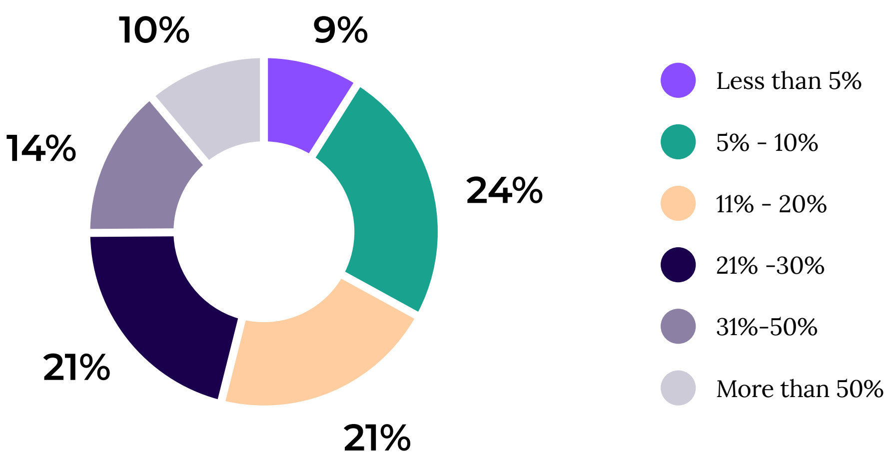
Fails and interventions

There is significant scope for error in complex modern derivatives markets. Failed give-ups, brokerage reconciliation and collateral and margin movement are all key potential points of weakness in the day-to-day of post-trade.

Sixty six percent of surveyed firms said that their listed derivatives operations teams were spending more than 10% of their time resolving post-trade exceptions, fails and settlement breaks – including margin call disputes and reconciliation breaks.

Twenty four percent said that this constituted more than 30% of their time, which represents a major drain on resources. The cost of dealing with these problems can be high. Not only do staff hours become bogged down in unproductive manual tasks that reduce the capacity for higher value work, but the higher frequency of manual intervention also elevates the risk of further mistakes.

Approximately, what percentage of your listed derivatives operational team's time is currently dedicated to resolving post-trade exceptions, fails, and settlement breaks including margin call disputes and reconciliation breaks?

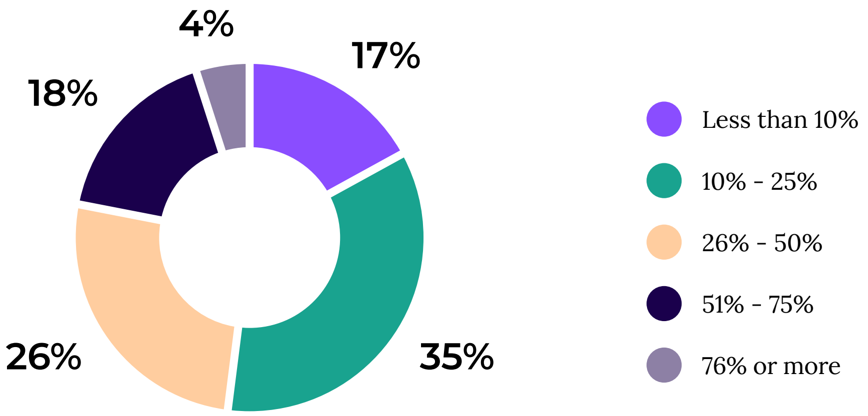


In bilateral OTC derivatives, a significant sweep of the market is still uncleared and instruments are less standardised than listed products.

Here, surveyed firms reported more of a manual drag on their operations. Eighty two percent of survey respondents said that more than 10% of their bilateral OTC derivatives trades were confirmed manually rather than electronically.

For nearly half of respondents (47%), over a quarter of their bilateral OTC trades were confirmed manually. The delay that this high level of manual intervention entails has direct consequences for timeliness functions such as margin calls and portfolio compression.

Approximately what percentage of your bilateral OTC derivative trades are confirmed manually (rather than electronically)?

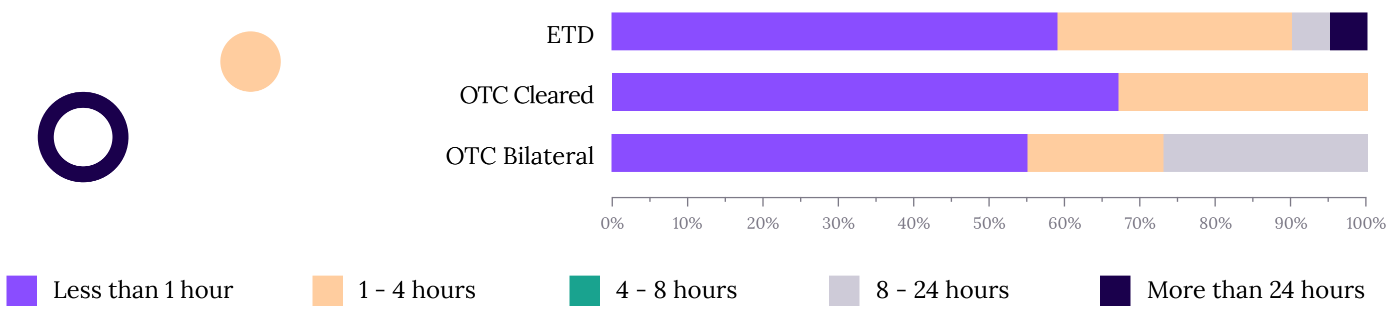


While these issues directly affect the back-office, they also seep into front-office activity. As firms across derivatives markets focus more acutely on all contributors to a trade, from choice of venue to collateral efficiency, recognition is growing of the role that post-trade can play in creating broad trade lifecycle efficiencies.

Same-day settlement

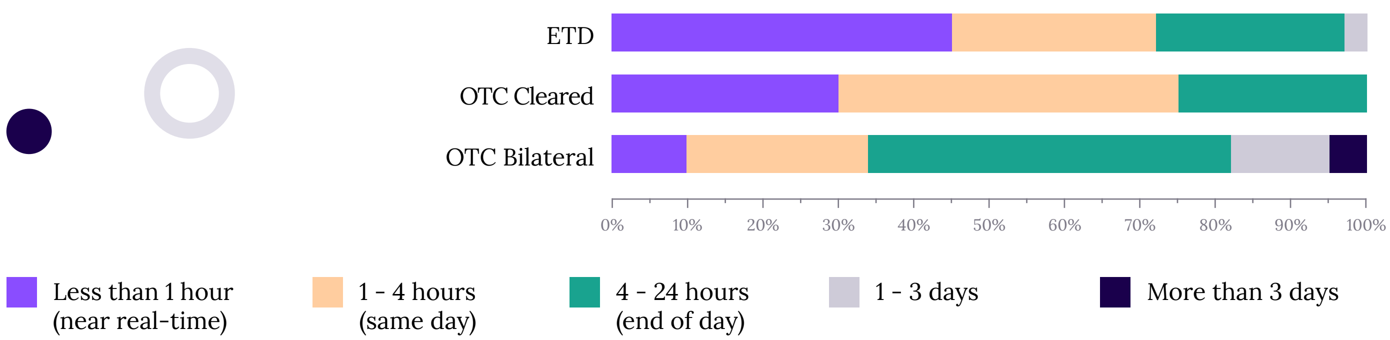
While the operational headaches that trade fails and manual intervention cause are significant, they can also consume capital resources. Trade breaks, give-up breaks or allocation breaks can land an unwanted trade on a dealer's balance sheet overnight and consume capital. Even on an intraday basis, trade affirmation delays can also create unhedged market exposure. Among those respondents with access to the actual figures, most estimated that this averaged less than an hour, but 42% said that their ETD exposure could go unhedged for more than an hour due to uncertainty in trade affirmation and confirmation processes.

On average, how many hours of unhedged market exposure are created by delays in trade affirmation and golden record creation at your firm?



These risks have increased the importance of shortening the time between trade execution and settlement as much as possible. In a sign of the benefits of recent investment, most surveyed firms can now achieve this on an intraday basis for the asset classes that they cover. In OTC bilateral markets, processing was slower, although most were able to create a golden record by end of day. While a minority, the 14% of firms that take one to three days to achieve an authoritative golden record on their bilateral OTC trades is significant. In a T+1 regime, delays of this length equal failure to make the settlement window for a notable proportion of the market.

On an average day, what is the approximate time delay between trade execution and achieving a golden record?



These efficiencies also highlight the growing importance of same day, or T+0 settlement. While creating a tighter deadline for firms to work to, the protocol can significantly reduce the capital implications of issues like settlement or give-up failure.

Failure to resolve this part of the trade lifecycle and close a trade on a same-day basis can leave a position open and push two counterparties into posting margin on a position that should be closed.

Few markets have mandated widespread T+0 settlement yet, with most firms that work to the cycle doing so on a voluntary basis and having made the necessary investments to support it.

Data quality

The crux of any successful trading operation is data quality. It is on this basis that systems can run smoothly, reconciliations be performed effectively and synergies be realised, where possible.

Data quality is also increasing in importance as more firms launch artificial intelligence projects to drive efficiencies across operations. This can range from rationalising execution desks' trading limits to risk management in the middle-office. Regardless of its purpose, the success of any AI project will be determined by the quality of the data that it can feed on.

Given the size and complexity of most legacy post-trade systems, extracting and rationalising data can represent an enormous task. However, across derivatives markets, awareness is spreading that it is a necessary one to stay competitive.

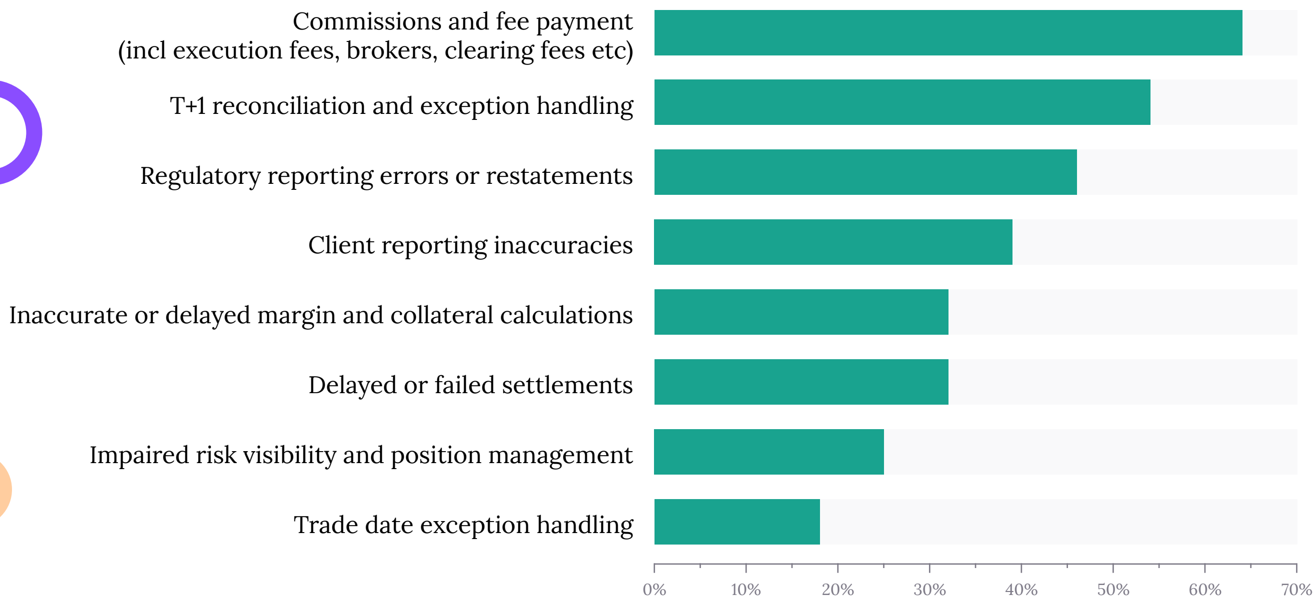
As well as creating the foundation for future competitiveness, data quality is also essential for smoother day-to-day operations. The pain points that poor data quality causes tend to create a lasting drag on operations, rather than the risk of a dramatic blowup.

The example of commissions and fee payment, which firms cited as the biggest pain point, is illustrative. Charging correct fees entails a complicated process of brokerage reconciliation whose inputs consist of bespoke and negotiated reference data. Data quality is essential to correctly calculating these fees, with incorrect entries leading to breaks.

Fees charged in a derivatives transaction range from execution commission, to clearing fees, to exchange and CCP fees, and often include give-up fees. Each firm involved in the transaction will use their own rate card for each trading relationship they maintain, which is used to calculate fees along with other details of the trade, such as size and product type. The process is liable to exceptions and unresolved breaks, which hold up payment of fees.

With buy-side firms now using a higher number of clearing and execution brokers, and give-up arrangements commonplace, the number of counterparties needed to take part in trade reconciliation has grown, creating further complexity.

In which of the following areas does poor trade data quality create the greatest operational or financial impact at your firm?
(Select top 3)



Similarly to fees, T+1 reconciliation and exception handling, ranked second, is a high-volume and exception-driven process where incorrect or stale data requires manual intervention. It is also the rhythm that markets increasingly move to under regulatory mandates. The US, Canada and Mexico transitioned to T+1 settlement in 2024, while the UK, EU and Switzerland are preparing for a 2027 implementation.

While set to drive greater efficiency across markets, T+1 settlement has also created challenges for post-trade processing. By shortening the settlement cycle, the margin for error in trade matching, affirmation and golden record creation has significantly shrunk.

As highlighted earlier, squeezing these processes into a shorter cycle can carry significant consequences for hedging, capital efficiency, reduced liquidity and worse responsiveness to clients.

Regulatory reporting errors were also commonly flagged as pain points. This has been an operational sell-side headache for some years, especially with the roll out of regulatory requirements such as the EMIR Refit. Submitting regulatory reports is a data challenge in itself, with reporting teams having to interpret multiple different fields.

Tasks such as reconciliation become even more high stakes when failure carries the risk of external investigation and fines for incorrect reporting. After an initial period of frustration, when many firms felt that they were sending regulators swathes of data that the latter were unable to analyse, authorities have much improved their toolbox for dealing with these problems and have thereby been able to increase their demands for high data quality from firms.

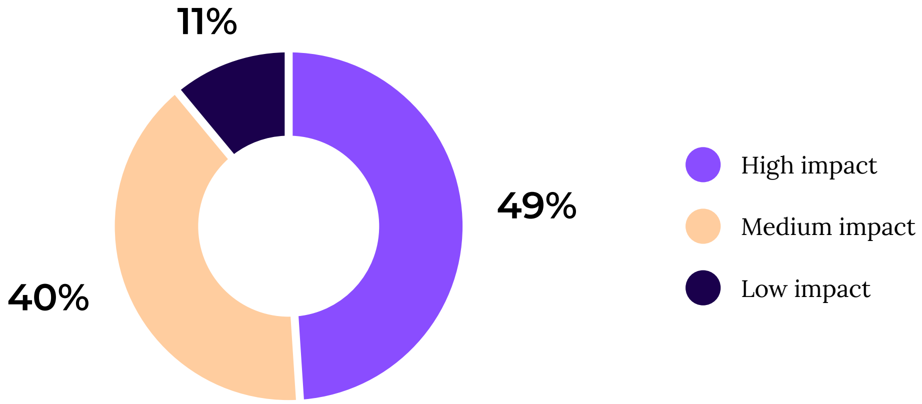
Survey respondents also cited issues in surveillance issues and client money as being created by poor trade data quality.

Capital efficiency

Capital relief through post-trade

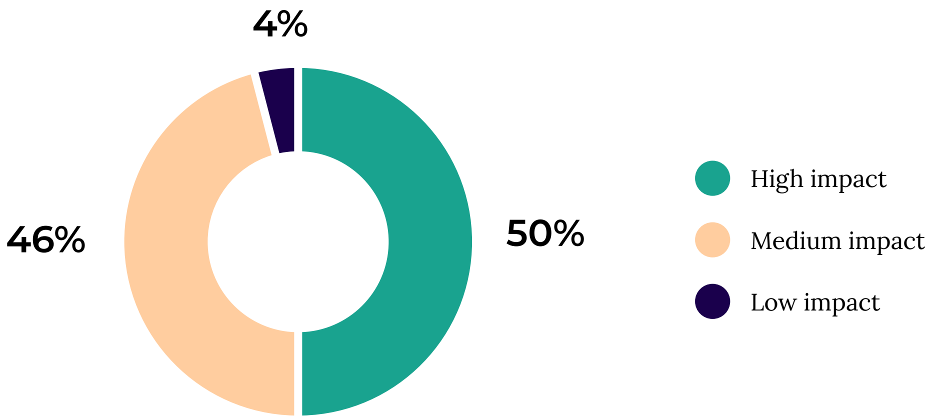
Industry awareness is growing around the capital efficiencies that post-trade investment can create. With more buy-side clients conducting deep analysis of their margin efficiencies, the frequency of porting clearing portfolios between FCMs for commercial, not default, reasons, has been increasing. For client clearers, this can represent a new source of risk, as clients moving a portfolio in pursuit of margin offsets can create a margin add-on just as easily as an offset for their clearing broker. Eighty nine percent of surveyed firms said that better post-trade netting and optimisation within listed derivatives would have a noticeable impact on their firm's balance sheet efficiency and capital requirements, with 49% saying it would be a high impact.

How significant would the impact of better post-trade netting and optimisation within listed derivatives be in terms of improving your firm's balance sheet efficiency and capital requirements?



For OTC derivatives, optimism was even higher, with 96% foreseeing a noticeable impact and half saying this would be high impact. While significant portions of the OTC markets are now cleared, in this respect the market is much less mature than listed derivatives. The latter product group has always been linked to central clearing and long enjoyed the benefits of multilateral netting. OTC instruments, however, are a much less standardised and optimised product, so have greater capacity for increasing efficiencies.

How significant would the impact of better post-trade netting and optimisation within OTC derivatives be in terms of improving your firm's balance sheet efficiency and capital requirements?

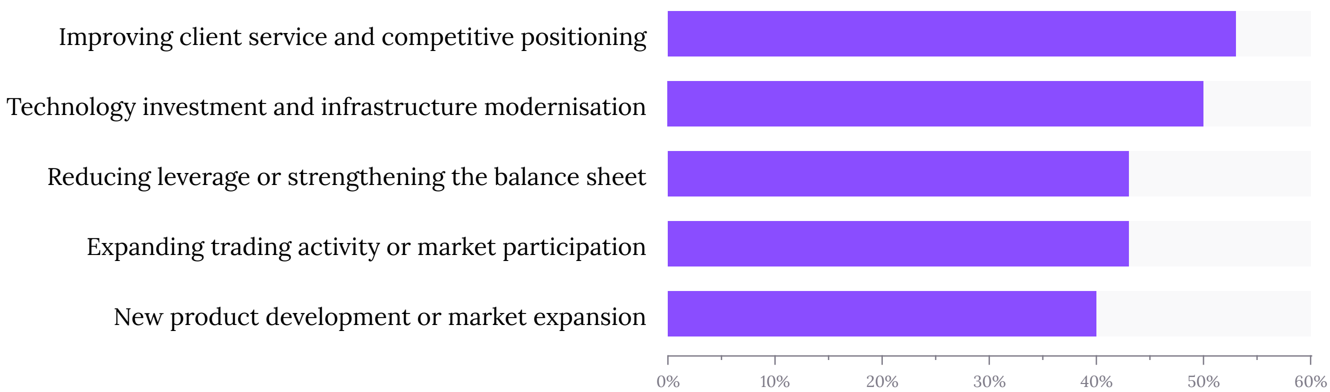


The positives of capital relief on a sustainable basis can be wide-ranging and long-term supportive of business objectives. The main advantages that firms foresaw were improved client service and competitive positioning, as well as technology investment and infrastructure modernisation.

These are both areas with direct feed through to alpha generation, especially the benefits to client service and competitive positioning. Being able to allocate capital to other areas of the business, such as the front-office is an important competitive advantage, especially in an environment characterised by often onerous and inflexible buy-side demands.

For example, the connectivity needed to win a systematic hedge fund's business will typically involve offering access to a complete suite of products across multiple venues, which can represent a very high cost base, especially in a fragmented market such as Europe or APAC. Freeing up capital from the back-office can therefore support the high costs needed to win high revenue clients.

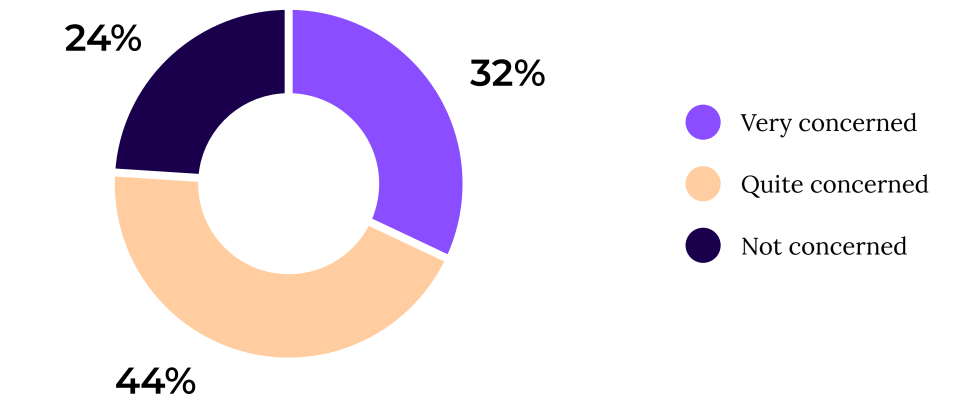
If your firm were able to free up capital currently trapped in inefficient post-trade processes, how would you prioritise its deployment?



The regulatory shadow

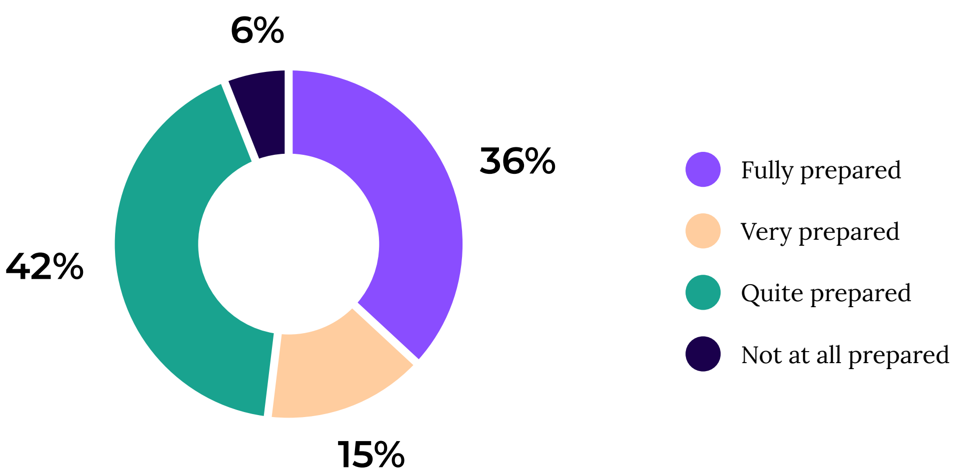
It should be noted that regulation still presents an ever-present risk of raised capital requirements in the minds of many firms. Just over three quarters of surveyed firms were worried about the effect that regulatory updates such as Basel IV, the G-SIB surcharge and Uncleared Margin Rules could have on their capital requirements. Almost a third said that they were very concerned.

How concerned is your firm about increased capital requirements under evolving regulatory frameworks (e.g., Basel IV, G-SIB surcharge, UMR)?



Post-trade teams have had to deal with other regulatory demands in recent years. Rules introduced under DORA (EU) and SR 11-7 (US) have obliged market participants to undergo extensive analysis of their post-trade systems and vendor relationships. While challenging, this has actually proved to be a good news story for compliance. Most firms were well prepared for these frameworks' requirements to cover "extreme but plausible" operational disruption scenarios, with 36% fully prepared.

How prepared is your firm for "extreme but plausible" operational disruptions in post-trade processing, as required under DORA, SR 11-7, or equivalent frameworks?



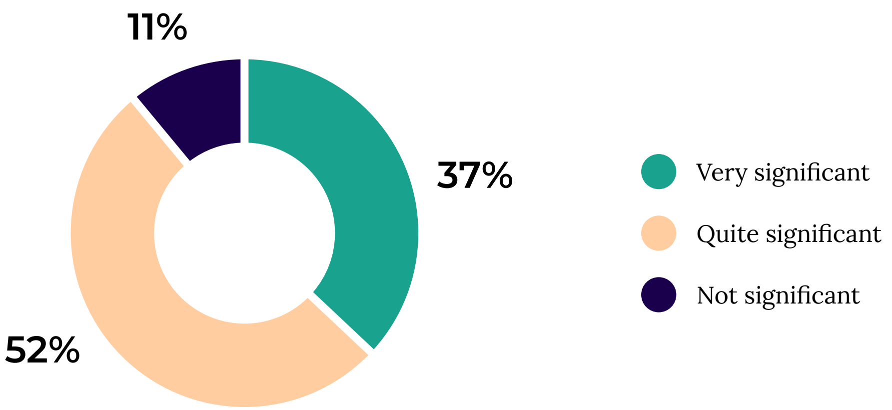
Driving the competitive edge further

The benefits of post-trade improvement are not limited to capital, however. As described in section one, post-trade infrastructure that speeds up settlement and optimises collateral can not only deliver benefits for back-office teams, but also free up front-office capacity.

Given the complexity of modern markets, with their array of trading venues and clearing houses, analysing the full cost of a trade has become a much more complicated task for trading desks and in many aspects goes beyond the original responsibilities of a trader. A post-trade operating model that optimises CCP margin, capital and collateral can deal with that complexity after the trade and free up front-office time to focus on market movements.

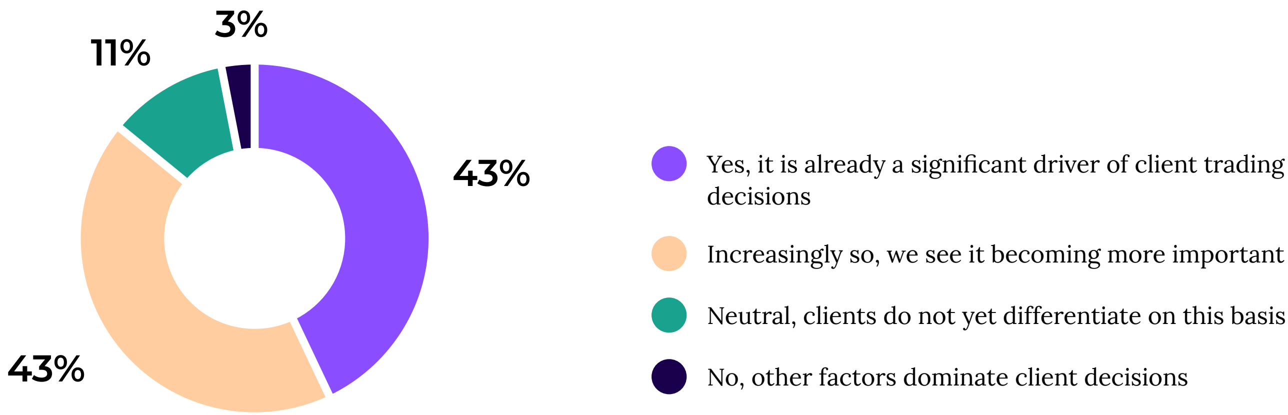
Firms also recognise liquidity and resource management benefits from increased post-trade efficiency. In a market environment of high funding costs and tightening liquidity, cash that is locked up in excess collateral or intraday cash holdings can create a notable drag on a firm's ROE. Eighty nine percent of survey respondents saw the gains in this area as significant, capturing the growing view of post-trade as much more than a passive processing centre, with benefits such as faster settlement, reduced margin drag and optimised collateral deployment.

How significant is the liquidity and resource management benefit your firm could gain from improvements to post-trade efficiency (eg through faster settlement, reduced margin drag and optimised collateral deployment)?



In fact, most firms saw faster, more transparent and more automated post-trade offerings as a significant competitive advantage when dealing with their institutional clients. Forty three percent said that this was already a significant driver of client trading decisions, while the same proportion said they were recognising its increasing importance.

Does your firm view superior post-trade transparency, speed, and automation as a key competitive differentiator when servicing institutional clients?



Buy-side recognition of post-trade opportunities

While sell-side recognition of the benefits of post-trade optimisation are widespread, there is also recognition of its merits among the buy-side. Through interviews with buy-side representatives, we found a serious focus on the importance of optimisation. This covered both buy-side optimisation tools and the quality of service from sell-side firms that use optimisation for their post-trade.

This is relevant at a broad-level, in terms of sell-side firms with more available capital being able to provide more client-friendly services such as prime brokerage leverage and broader coverage of financing for different asset classes.

However, there is also a more granular recognition of the benefits of optimisation in its own right, as hedge funds seek to optimise their own balance sheets by netting similar positions across funds or pods through their prime brokerage relationships, for example.

This in part results from a greater focus on capital efficiency and optimisation at hedge funds themselves. More and more client-led conversations about margin optimisation and collateral management are taking place between hedge funds and their sell-side counterparties.

Crucially, clients are also demanding good quality data from their sell-side relationships to be able to scrutinise how well optimised their own trading operations and relationships are. With transaction cost analysis an ever increasing part of market activity, such data come from the back-office as much as the front and is not just a nice to have, and only serves to confirm why forty three percent of surveyed banks and brokers said that this was already a significant driver of client trading decisions.

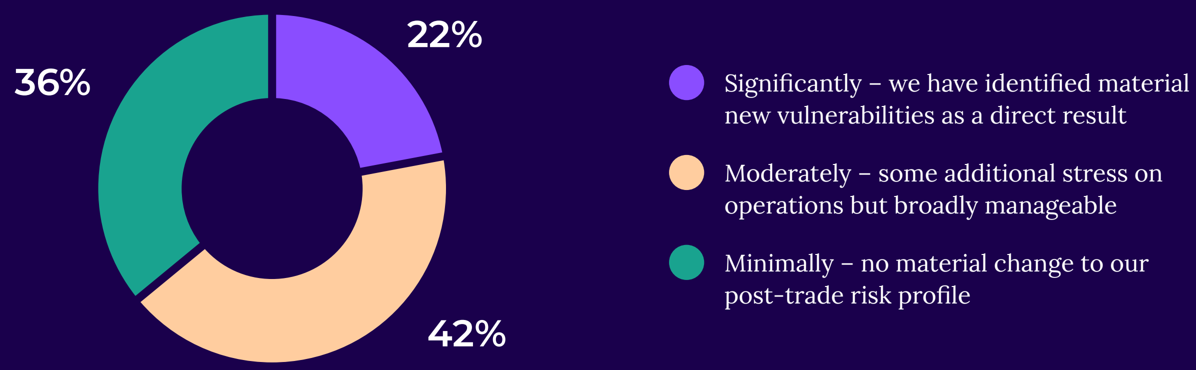
Determining the path forward

Navigating geopolitics

The increasing geopolitical risk that has affected most industries in the global economy also carries challenges for post-trade. Geopolitical risk creates market uncertainty and often volatility, which commonly not only drives higher volumes, but also higher margin calls, hitting trade limits and counterparty credit risk.

This will take place in a market structure that already creates high levels of margin exchange. Most survey respondents said that geopolitics have increased their operational risk to some extent, although more said that the stress on systems had been manageable for the most part.

To what extent has the current geopolitical environment increased operational risk and exposed vulnerabilities in your firm's post-trade infrastructure?



Planning investment

One of the key findings highlighting the transformative potential of better post-trade processes was that 50% of firms said they would free up capital trapped in inefficient post-trade processes to deploy it into technology and infrastructure modernisation.

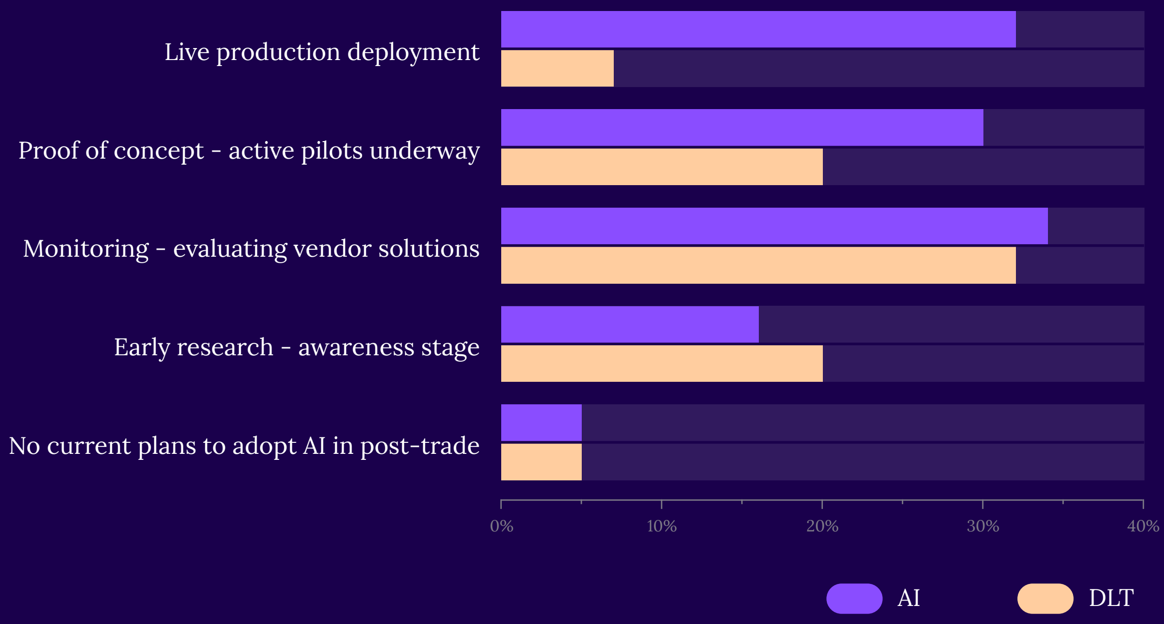
Once this capital is unblocked, a key area of technology modernisation is AI: Nearly a third of firms said they were in live production deployment of AI in their post-trade operations. A similar proportion were at the proof-of-concept stage, with active pilots underway.

Adoption of AI ranked much higher than distributed ledger technology, the other technology with transformative potential for the financial industry. This can be attributed to the wider reaching scope of AI across teams, with most management teams trying to apply the technology as much as possible in their teams' day-to-day responsibilities.

The fact that 32% of firms are already live on production deployment of AI, as opposed to 7% for DLT, which has been an available technology for much longer, is telling. While DLT also offers significant efficiencies, its applicability is much more focused in areas such as collateral mobility and rapid settlement, as compared to the broader sweep of AI.

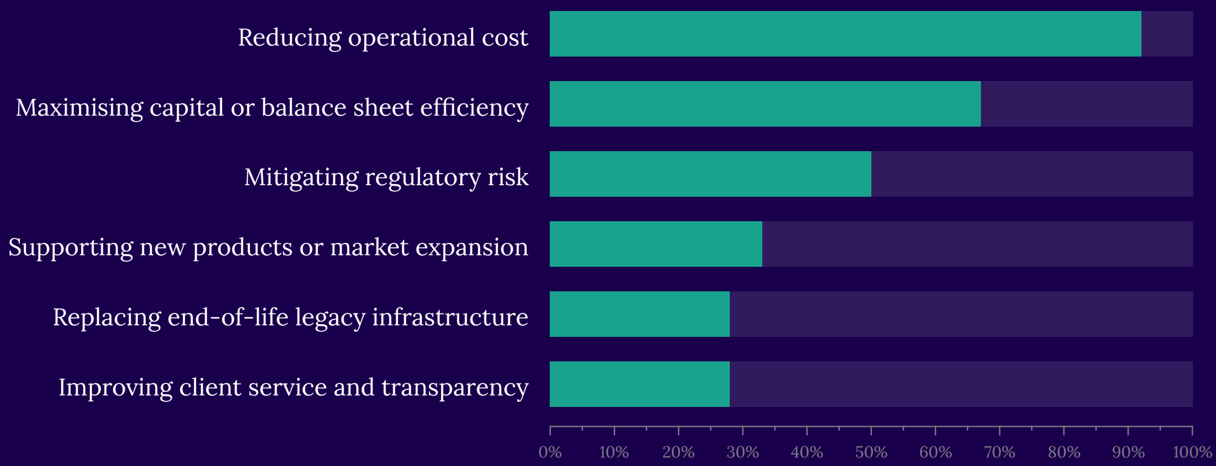
The application of DLT to post-trade also relies on wider industry collaboration, while AI can be rolled out within firms for internal processes without relying on a network effect or shared processes.

How is your firm approaching the adoption of Artificial Intelligence and DLT in post-trade operations?



Over an 18-month horizon, firms listed reducing operational cost as their main motivation for investing in post-trade technology. They also ranked maximising capital or balance sheet efficiency highly. This not only reinforces the importance of this channel for achieving capital efficiencies, but also shows how widely recognised optimisation has become as a mechanism for capital and balance sheet efficiency. Especially in a regulatory environment where firms report a high risk perception of increased capital costs under the incoming Basel IV framework, G-SIB surcharge and Uncleared Margin Rules, the need to get in front of any such regulatory events is important for many firms.

What are your firm's top motivations for investment in post-trade technology solutions over the next 18 months?



Conclusion

The pace of change that the derivatives industry and its post-trade sector have had to deal with in recent years has been accelerating. Not only have market conditions jump started to a new volatility regime, but regulation and industry trends have also created a much more complex market structure than existed even a decade ago.

Post-trade operators have recorded significant successes in these years, reversing an underinvestment trend and pushing to embrace new technologies that further reduce operational risk. The sector now stands at a moment of unique opportunity, with AI in particular offering the chance to leverage new efficiencies at pace.

Firms are clearly alive to the benefits of post-trade efficiency and how widely they can support an organisation. Principal among these is capital relief, which more firms are realising can be powered by hidden post-trade alpha, unlocking investment dollars across their firm.

In addition to this, there is a clearly identifiable competitive edge that firms can create in the front-office through post-trade investment. Building infrastructure that deals with the complexity of modern trading and takes on optimisation responsibilities for the front-office is increasingly recognised as a differentiator with clients.

So, while plenty of challenges lie in the future, post-trade practitioners are also approaching an era of new opportunity that could redefine the significance of their sector to the wider derivatives industry.

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