The post-trade revolution: transforming the ability to manage liquidity and risk

Alex Knight, head of Europe, the Middle East and Africa at Baton Systems, explores the ongoing technological revolution in post-trade processing that consigns the problems of inefficient, costly and restrictive processes to the past

An unprecedented transformation is taking place right now across the entire FX post-trade landscape. Banks are starting to take advantage of the latest technology to address some of the fundamental challenges faced today: declining margins, the pressure to generate adequate capital returns and the growing value of FX trades subject to settlement risk.

However, many firms continue to operate ageing, server-based, hard-wired and inflexible post-trade infrastructures. These drain limited human and financial capital. So why are they still so prevalent? Because ripping out and replacing existing legacy infrastructure just isn't an option.

These same firms are acutely aware that market developments unfolding, as we speak, will necessitate a radical shift in their existing post-trade infrastructures. Take, for example, the need to more effectively manage settlement risk against a trajectory of growth in emerging market currency trading, or the imminent progression towards the need to process a far broader range of assets (including digital and fiat). These firms know they need to act now and what they have in place today simply won't deliver the prerequisite security, extensibility and flexibility attributes they'll soon require.

Importantly, there are solutions available today that will allow firms to take advantage of the latest developments in post-trade processing and embrace industry developments. Offering significant performance and risk management benefits, these solutions actually work with the legacy post-trade systems and processes banks already have in place, to deliver fully digital market infrastructures.

Driving business performance and reducing risk

Considering existing financial, competitive and regulatory pressures, there is an urgent need to deploy post-trade infrastructure that enables banks to reduce their operational cost bases, manage down intraday liquidity usage (and funding costs), reduce settlement risk (and capital usage) and eliminate failed settlements and errors. In other words, what is needed is a transformation that will considerably enhance both top and bottom lines, and drive an improved return on capital and reduction in risk.

To address this challenge, firms need to move away from legacy, siloed, queue-based and asynchronous payments processes in favour of a more controlled and transparent approach. With smart workflows (activated by real-time data) operating across interoperable distributed ledgers, these new solutions place settlement participants in the driving seat with an unparalleled level of visibility across all activities. Offering full control over the choice of netting and payment strategies deployed, the entire process from trade matching through to settlement can be automated. Adopters can collaborate with their settlement parties, and even agree at what time they'll settle, so it's aligned with their funding requirements.

Responding to the revised *FX Global Code*

Regulators are starting to pay greater attention to settlement risk. The Global Foreign Exchange Committee's updated *FX Global Code July 2021* ("the Code") increased its emphasis on this area – requiring signatories to reduce settlement risk exposure and use payment versus payment (PvP) settlement mechanisms where possible.

The language used is far more prescriptive than before, reflecting that the technology now exists for the principles set out in the Code to be realised. Baton's Core-FX solution, for example, is available to all market participants and across all currencies. Offering the functionality to complete the entire settlement process in under three minutes, Core-FX allows banks to safely settle their FX trades with the security, certainty and finality of PvP.

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> Alex Knight, Baton Systems

The importance of interoperability

Interoperability will be fundamental in ensuring that new technologies work seamlessly with those already in existence and will easily connect with future additions – such as those likely to be deployed to support the processing of new asset types. Baton's rules-based distributed ledger forms the backbone of Core-FX, and has been specifically designed to interoperate with the multitude of systems and processes banks already have in place, including core ledgers, payment gateways and messaging systems.

The future of post-trade is already here

The revolution in post-trade processing is now well under way. The technology exists today to allow banks to eradicate the status quo of inefficient, costly and restrictive post-trade processes. With the introduction of fully digital market infrastructures from trade matching through to settlement, adopters can now effectively control the movement of cash and securities across the entire front-to-back post-trade process.

Interoperability is swiftly removing previous roadblocks and allowing banks to achieve fully connected, friction-free, flexible and transparent processing.

As a result, an unprecedented opportunity now exists for firms to redesign and upgrade their post-trade environment without the risk of a rip-and-replace project. In doing so, they can deploy post-digital solutions designed to reduce risk exposure, eradicate unnecessary costs and enhance key capital and liquidity metrics. FX