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Chart in focus

March 3, 2023

OTC derivatives trading

First signs of a shift from London towards EU financial centres

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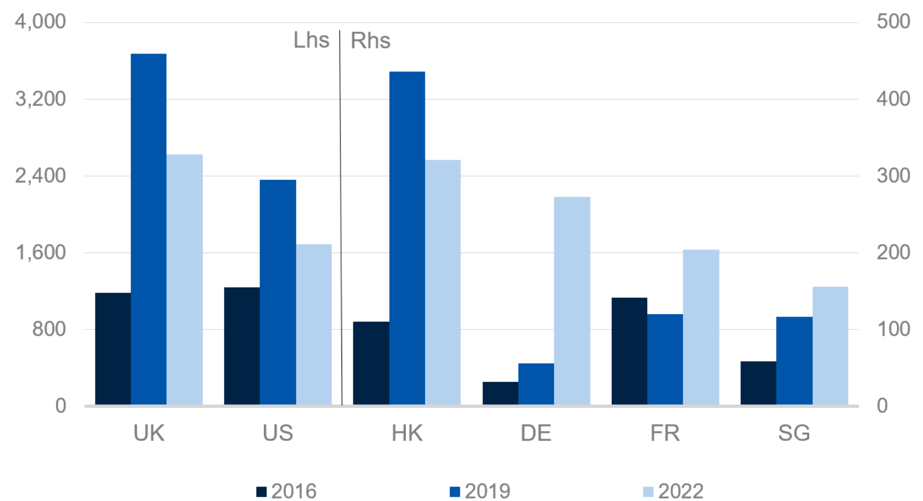
London continues to be the leading trading hub for OTC interest rate derivatives with a market share of 46% and an average daily turnover of USD 2.6 tr. However, the UK has lost ground since 2019 when its market share was still 51%. This is due to the transition away from Libor as well as the ongoing efforts of EU authorities to bring more derivatives clearing into the bloc.

OTC derivatives trading: First signs of a shift from London towards EU financial centres

Interest rate derivatives, average daily trading volume in USD bn



Sources: BIS, Deutsche Bank Research

The derivatives market is characterised by its enormous size, global nature and strong concentration on major financial centres like London. The outstanding notional value of over-the-counter (OTC) derivatives amounted to USD 632 tr at the end of June 2022, according to BIS statistics. Derivatives allow hedging against risks such as interest rate risk, exchange rate risk or fluctuating commodity prices. Interest rate derivatives are the most important category, representing about 80% of the outstanding notional value. Moreover, the top-6 trading locations shown in the chart account for 91% of the global trading volume.

London continues to be the leading trading hub for OTC interest rate derivatives, as the latest BIS Triennial Survey shows. In April 2022, the UK registered an average daily turnover of USD 2.6 tr on a “net-gross” basis.[1]

This corresponds to a market share of 46%. However, the UK has lost ground since 2019 when its market share was 51%. There are two main reasons for this:

1. The transition away from Libor has led to a decline in the global daily turnover from USD 7.3 tr in 2019 to USD 5.8 tr in 2022 on a "net-net" basis (-19%). Notably, the average daily turnover of forward rate agreements (FRAs) shrunk to USD 0.5 tr, down from USD 1.9 tr in 2019. FRAs are used to hedge the floating rate risk of swaps referring to the Libor rate. However, they lost much of their relevance as, since January 2022, contracts in several major currencies (GBP, EUR, CHF, JPY and some USD contracts) no longer refer to Libor, but to overnight risk-free rates. The decline in FRA turnover decisively contributed to lower trading volumes in the UK, the US and Hong Kong.
2. However, the UK also saw a decline in non-FRA instruments (swaps and options). In April 2022, their average daily turnover stood at USD 2.3 tr on a "net-gross" basis, representing a market share of 43%, down from 52% in 2019. On the one hand, this is because turnover of euro-denominated contracts decreased to USD 1 tr in 2022 (-18%). At the same time, in the euro area, turnover of such contracts almost tripled to USD 359 bn. Particularly striking was the rapid growth in Germany, i.e. Frankfurt, where turnover skyrocketed to USD 204 bn. On the other hand, the UK – as the only top-6 location – had a lower turnover of US-dollar denominated non-FRA instruments in 2022. Although this is just a first data point in a survey conducted every three years, these figures indicate a certain post-Brexit shift. Given Brussels' plans to further accelerate the shift of euro-denominated derivatives clearing to EU financial centres, the trend might well continue.

In December 2022, the European Commission revealed plans to strengthen clearing capacities in the EU and reduce the reliance on non-EU clearing houses. The proposed amendment of the European market infrastructure regulation (EMIR) would introduce obligations for EU market participants to (1) maintain an active account with an EU clearing house and (2) clear a fraction of derivatives deemed systemically relevant on EU clearing houses. The latter includes interest rate swaps in euro or Polish Zloty as well as credit default swaps and short-term interest rate derivatives denominated in euro. The fraction to be cleared in the EU will be defined by the European Securities and Markets Authority (ESMA). In the Commission's view, this fraction should be "proportionate" and consider the implications for the competitiveness of EU market participants. Furthermore, the proposal seeks to strengthen EU clearing houses by simplifying the processes to approve new clearing services and activities. The proposal has yet to be endorsed by the Council and the European Parliament, with negotiations not expected to start before the second half of this year. Until June 2025, UK clearing houses can continue to clear derivatives for EU counterparties under an extended equivalence decision.

[1] Figures on a "net-gross" basis have been corrected for local inter-dealer double-counting. They are used to compare developments in different locations. Figures on a "net-net" basis have been corrected for local and cross-border inter-dealer double-counting and are used to describe global aggregate market developments.

See also: Bank for International Settlements (2022). Triennial Central Bank Survey. OTC interest rate derivatives turnover in April 2022. October 27.

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