



TRADING TECHNOLOGY LTD

GODLIMAN HOUSE  
21 GODLIMAN STREET, LONDON EC4V 5BD  
TEL: 020 7253 5220 FAX 020 7689 3309  
INFO@TRADINGTECHNOLOGY.COM  
WWW.TRADINGTECHNOLOGY.COM

For immediate release,

## PRESS RELEASE

Paul Pickup, Director,  
Trading Technology Ltd.

Tel: 020 7253 5220  
paul.pickup@tradingtechnology.com

### ***T+1: Looks like it will never happen!***

**Paul Pickup, Director, Trading Technology Ltd**

Trading Technology recently concluded a study of leading global brokerages into the risks involved in reducing settlement cycles to T+1. The conclusions show that while everyone is caught up in the stampede for shorter settlement cycles, few have thought through the risks that this introduces, and even fewer have identified any benefit. Trading Technology argues that the aim of the regulators and central facilitators should be to reduce the complexity involved in the settlement process, and allow Straight Through Processing (STP), rather than merely tightening the settlement window.

Goutam Bose, Trading Technology's Director of New Markets, presented these points at the **Globalisation 3 Conference** on the 14th November in Amsterdam.

- **The timescales for T+1 are so long that it is in danger of cancellation.**
- **Brokers are “burying their heads in the sand” regarding the need for high-availability settlement systems.**
- **T+1 can only be achieved when central banks can process payments in real-time.**
- **Brokers will be forced to run 24-hour operations.**
- **The risks involved in going to T+1 are far greater than those going to T+0.**
- **Although T+1 may be achieved, there will be an unacceptable level of settlement failures.**
- **T+1 is at loggerheads with the current trend for netting with central counterparties.**
- **The benefits of T+1 are few; there are perfectly good mechanisms in place for covering the risks in T+3.**
- **GSTPA must succeed in facilitating cross-border transactions if T+1 is to be realised.**
- **T+1 can only be achieved with pre-allocation between buy-side and sell-side.**

Goutam Bose commented, "Everyone is missing the point. They are labouring under the belief that shorter settlement cycles are better. It is not the latency that needs to be addressed, it is the efficiency and complexity of the overall process".

Paul Pickup commented at the same event "The central facilitators and regulators have a responsibility to help brokers streamline the entire settlement process, both between the buy and sell side and for cross-border transactions. The GSTPA and Omgeo initiatives should be supported by the central facilitators." On the subject of a pan-European Clearing organisation, "Although a central European clearing organisation seems the simplest solution, it is naïve to expect the clearing houses to sort it out for themselves. The experiences of Euroclear Bank have shown that the merging of friendly organisations is difficult enough. What is needed is a network of clearing houses able to process both national and international transactions."

Further details of the survey finding and presentation to the Globalisation 3 conference.

### ***Is T+1 a poor relative to T+0?***

The shortening of the settlement cycle to T+1 will put intolerable strain on the established bureaucratic settlement processes. This is without delivering any notable business benefit. With any latency built in to the settlement process, there will be problems of cash flow management, margining, stock lending and risk management. These are made worse under T+1 as there is less time to identify risks and manage them. Only the utopia of real-time settlement will actually bring any benefits.

### ***The advent of the Global Day***

While it may be perfectly possible for national business to be settled in one day, it will be very different in global markets. If the client is in Hong Kong and instructs trades on the US markets, the concept of a trading day is lost. By the time the executions come back from the US market, the HK client will have gone home. Who will confirm the allocations?

Goutam Bose argues that this time difference really means "T+1 becomes T+1/2".

Although the GSTPA solution goes some way to solving the allocation process, it still requires both parties to be able to respond to post-trading events.

There will either be a need for pre-allocation standards and algorithms to be established, or for brokers to man 24-hour operations to confirm executions, and allocations as they happen around the world.

### ***Client Cash Collection***

Private clients will either need to deposit cash up front for executions, or Brokers will need to stretch credit limits in order to settle in time. Again this is

due to the delay caused by central banks in facilitating payments. This increases the risks for the broker, in addition to the cost of systems re-engineering.

### ***Banks not geared up for Continuous Linked settlement***

While the pace of technology quickens for central depositories, the central banks are far from ready for real-time payment. Many still operate on an overnight batch basis, which given the time zones that are operated on by the global banks, will cause latency in the settlement process. The problem is far greater where FX transactions are involved, being currently a two-day settlement process.

### ***System Costs – the need for the re-architecture of settlement processing***

In a recent survey of brokerage firms, only 40% were thinking about re-architecting their operations systems to be resilient to failure. While the current settlement process is three days, a 4-hour system outage is an inconvenience, but with T+1 it will be a disaster. Brokers are concentrating on the need to process transactions in online and away from batch mode, but they are ignoring or unable to deal with the risks involved in system failure. The cost for brokers to re-architect their applications is estimated to be \$3.3bn in the US alone, with a further \$2.9bn spent on standardisation. Yet there will be no discernable benefit for the brokers or their customers.

### ***Increased risks***

Rather than reducing risk by having shorter settlement periods, it is likely to be increased. If all your business goes “straight through”, there is a danger that this will apply to risk too, and it will be undetected. Nick Leeson managed to hide futures positions in back-books for months, irrespective of the settlement period. The most important point, says Mr Bose, are “the accounting points” in the process, and that the change needs to be led from this viewpoint in addition to a technical one.

Trading Technology are the only organisation to have developed a re-engineering program along these lines.

Finally, the duration of this particular project, now extended to 2005 in the US, is itself a risk. It is possible to calculate the probability of a project failing by its sheer longevity, the longer it takes, the greater the risk. T+1 is already a four year-plus project in the US, and thus has a high risk of being delayed indefinitely.

### ***Conclusions***

There is little point in racing towards T+1 without the central facilitators and industry bodies taking a step back to eliminate the existing bureaucratic processing in securities settlement.

The processes that induce latency of central banking payment, netting and order allocation need to be re-engineered in order to move towards near real-time settlement.

In this respect, the central facilitators should concentrate their efforts into ensuring the success of the streamlining process, such as those offered by GSTPA and Omgeo, rather than “turning the screws” on an already tight settlement cycle.

## ***Back ground to Trading Technology Ltd***

Trading Technology is a specialist consultancy in technology issues for central markets, and has an unbroken record of system delivery, incisive foresight and satisfied customers. Trading Technology is a good source of knowledge for best practises amongst exchanges, clearing houses and brokers.

Trading Technology Ltd works equally for the broker community and those serving them. Our main offerings are

- Project management for system implementations
- Business analysis, requirements definitions for solution provision
- IT marketing and strategy advice

For further details of Trading Technology’s services see [www.tradingtechnology.com](http://www.tradingtechnology.com)

Or contact:

Alastair Moyes, Business Development Manager.  
alastair.moyes@tradingtechnology.com

Paul Pickup, Director.  
paul.pickup@tradingtechnology.com

Tel: 020 7253 5220