

THE CLEARING CORPORATION OF INDIA LTD

Risk Management Department

Consultation Paper

Proposal for Introduction of Forward trading in Government Securities

1. Introduction

1. A Bond forward transaction refers to a transaction where the seller agrees to deliver pre-specified bonds to the buyer on a mutually agreed date, at the specified price and quantity. Unlike Bond futures, a bond forward contract is customized to meet the requirements of the two parties and is traded over-the-counter. A bond futures contract on the other hand, has standardized terms and is traded on an exchange, where prices are settled on a daily basis until the end of the contract.
2. Both bond futures and bond forwards are settled either by delivery of the bond on the settlement date or by way of cash settlement (settlement of the price differential).
3. Placed below is a proposal that presents how CCIL can facilitate the forward trading of government securities once the same is approved by RBI.

2. Proposal

We had informal discussions with a few market participants in the securities segment to understand the rationale for forward trading in Government of India securities and to assess their expectations if CCIL were to facilitate this. From our discussions it is felt that the primary demand for forward trading in Government of India securities comes from insurance companies. There are indications that subject to Regulatory approvals, if CCIL were to provide a facility for forward trading in government securities, then banks are also likely to participate in this market.

Based on these discussions and our analysis, the proposed road map for CCIL is outlined below:

2.1 Trade lifecycle

- 2.1.1 Clearcorp Dealing Systems Ltd. (a CCIL subsidiary) may consider providing members with a trading platform (RFQ) for forward trading in Government Securities. The proposed RFQ platform would support bilateral negotiations. All features of current NDS OM RFQ will be made available for forward trades.
- 2.1.2 Forward trading is proposed to be permitted in all ISINs eligible for trading in the secondary markets. Similarly, there would not be any restriction on the tenor of the trade.
- 2.1.3 Once the forward trades enter the settlement window for outright trades (i.e. on Settlement Date -1 day) these trades need to be taken up for CCP clearing with other cash market trades concluded / reported on NDS OM. All forward bond trades will be physically settled just like other cash market trades in CCIL's Securities segment.
- 2.1.4 There will be a provision to report such trades to TR. Data dissemination on CCIL website will be done as soon as it is matched in TR. Trade reporting shall be done by both the counterparties if it is between inter-bank participants and single side if one of the counterparty is a User. However, if the User wants to avail the CCP settlement services of CCIL, they can come through a Clearing Member (CM). In such cases, there will be dual reporting and the CM shall report the trade on behalf of the User.

2.2 Risk Management

- 2.2.1 To start with, forward trades shall be taken up for exposure monitoring in the Securities Segment when they enter the T+1 settlement window (i.e. on S-1 day).
- 2.2.2 In the Securities Segment, trades are processed on a real time basis on the trade date itself. However, if a trade that has trade date falling before the current business date were to be received for processing, such a trade would be subject to both Initial

Margin as well as Mark to Market Margin at the point of acceptance. In line with this, the forward trades entering the securities segment will be subject to IM as well as MTM margins.

2.2.3 In the securities segment, if the acceptance of a trade for clearing, results in a margin shortfall, then a margin call is made to the members.

2.2.4 However, for government bond forwards, if on entry into the Cash Securities segment, such trades were to result in a margin shortfall for either counterparties, the trades shall not be accepted for clearing and remain in “pending acceptance” status. If the concerned member(s) fails to make additional margin available till the settlement day, the trade shall be settled bilaterally between the counterparties.

2.2.5 A product can be considered for CCP clearing only if there is adequate liquidity and depth in the market. Once market volumes in Bond Forward trades pick up, CCIL shall examine the possibility of offering CCP clearing services for such forward trades from the trade date. This would entail putting in place a separate risk management process (not part of this consultation).

3.0 Members are requested to send their suggestions and feedback on the above proposal. The feedback may be sent to us latest by 17th Sep’21 at rmd@ccilindia.co.in for attention of Chief Risk Officer, CCIL with Header as “*Consultation Paper: Forward Trading in Government Securities*”.

In case you require any clarification, please feel free to contact Mr. Kausick Saha, Chief Risk Officer on 61546441 or Mr. Nandan Pradhan, VP, Risk Management Dept. at 61546422.
