25 November 2011

Via Email: baselcommittee@bis.org

Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Dear Sir,

FEEDBACK ON BASEL COMMITTEE ON BANKING SUPERVISION'S SECOND CONSULTATIVE DOCUMENT ON CAPITALISATION OF BANK EXPOSURES TO CENTRAL COUNTERPARTIES

1. We refer to the second consultative document in relation to the capitalisation of bank exposures to central counterparties released by the Basel Committee on Banking Supervision ("BCBS") on 2 November 2011.

2. We appreciate that BCBS has incorporated a significant portion of the feedback provided to the first consultation, and welcome the opportunity to submit our comments on the second consultative document. Our response to the consultative document is attached.

3. If you require further clarification, please do not hesitate to contact Mr Zhang Changhao (Email: changhao.zhang@sgx.com) or Ms Wee Cheng Sim (Email: cheng_sim@sgx.com).

Yours sincerely,

AGNES SIEW
HEAD, CLEARING RISK
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SECOND CONSULTATIVE DOCUMENT ON
CAPITALISATION OF BANK EXPOSURES TO CENTRAL COUNTERPARTIES

SGX Comments

25 Nov 2011

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1 INTRODUCTION

1.1 Singapore Exchange Limited ("SGX") appreciates that Basel Committee on Banking Supervision ("BCBS") has incorporated a significant portion of the feedback provided to the first consultation, and welcomes the opportunity to submit its comments on the second consultative document issued in November 2011.

1.2 SGX operates two central counterparty ("CCPs") entities in Singapore, namely the Singapore Exchange Derivatives Clearing Limited ("SGX-DC") and the Central Depository ("CDP"). SGX-DC provides clearing services for exchange-traded derivatives contracts and over-the-counter ("OTC") commodities and financial derivatives contracts. CDP provides clearing services for securities and security-based derivatives contracts. The two clearing house entities are regulated by the Monetary Authority of Singapore as designated clearing houses under the Securities and Futures Act of Singapore.

2 COMMENTS

Greater recognition of netting benefits for CCPs

2.1 We appreciate that BCBS has recognised that Current Exposure Methodology ("CEM") may underestimate the multilateral netting benefits arising from a CCP, and has consequently raised the netting level to 70% from 60% under Paragraph 116(i).

2.2 This increase, however, has not yet incorporated the fact that CCPs may have much stronger netting rights than banks, where it is specifically carved out under the law. In

such cases, the CCP's default proceedings take precedence over the usual laws of insolvency. This greatly reduces the likelihood of unbundling by a liquidator.

2.3 SGX is of the view that the benefits of netting can be better recognised, i.e. up to 100%, for members where it can be established that the risk of unbundling is legally remote.

Net-Gross-Ratio definition should be refined for the CCP context

2.4 In order to compute the Net-Gross Ratio ("NGR"), the prescribed CEM assumes a bilateral context where trade exposures are accumulated. However, many CCPs mark-to-market the positions several times a day, and settle at least once a day. Contract prices are reset to settlement prices and there is no accumulation of exposure. Under the existing definition, NGR will be measured inappropriately using a single day of market price changes. This will cause unstable capital requirements.

2.5 To apply a consistent and appropriate approach for measuring NGR in the CCP context, our suggestion is to use the average daily NGR over a period of 3 months. Each day's NGR should be computed using the net daily MTM P/L, divided by the gross daily MTM P/L. The averaging effect will provide stability in the NGR number, and ties-in with the required reporting frequency.

Flat rates applied by CEM are unsuitable for calculating potential future exposure

2.6 SGX is concerned with the application of the flat rates specified by broad buckets of asset class and maturity for computing exposure. Firstly, these rates lead to inaccurate profiling of risk and penalises CCPs that clear contracts with relatively low volatilities. Secondly, we understand that the flat rates are calibrated for bilateral trades and hence inconsistent with the risks faced by CCPs.

2.7 Instead of flat rates, we recommend that BCBS specifies the parameters in terms of appropriate confidence level, holding period, and lookback period. CCPs may then determine the rate, taking into account the volatility and characteristics of each product.

2.8 Alternatively, BCBS could specify the flat rates to greater granularity, to the individual product level (e.g. index futures and options, single stock futures and options). The rates should also be re-calibrated to appropriate liquidation periods, given that CCPs have default management procedures and practice daily margining.

3 CONCLUSION

3.1 SGX would like to thank BCBS for the opportunity to participate in the consultation process. Please do not hesitate to contact Mr Zhang Changhao (Email: changhao.zhang@sgx.com) or Ms Wee Cheng Sim (Email: cheng_sim@sgx.com) if you have any questions. We look forward to be involved in future public consultations.