Centrally clearing the US Treasury market

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Central clearing of Treasuries transactions is still limited

Figure: Data gathered by Treasury Market Practices Group (2018) imply that a firm faces FICC on about 22% of Treasury transactions.
Broad central clearing
Broad central clearing reduces settlement commitments

14 are $684 billion (67%) and $760 billion (69%), respectively. Moreover, the correlation across days between the level of settlement obligations under the current structure and the reduction in such obligations with market wide central clearing is 0.71.

Figure 6 – Dealers’ Gross Settlement Obligations if All Trades Centrally Cleared

Source: Authors’ calculations, based on FINRA TRACE data.

Note: The figure plots dealers’ gross settlement obligations in U.S. Treasury securities by day under a potential structure in which all trades are centrally cleared and netted.

Figure 7 – Dealers’ Gross Settlement Obligations by Market Structure

Source: Authors’ calculations, based on FINRA TRACE data.

Note: The figure plots dealers’ gross settlement obligations in U.S. Treasury securities by day under the current structure in which dealers’ interdealer trades are centrally cleared and netted and under a potential structure in which all trades are centrally cleared and netted.

Figure: Source: Fleming and Keane, Federal Reserve Bank of New York, April 2021.
Central clearing reduces settlement fails

Figure: Settlement fails in treasury securities transactions involving primary dealers, and centrally cleared settlement fails at FICC. Data sources: Federal Reserve Bank of New York and FICC.
Central clearing reduces daisy-chain fails

Fleming and Keane (2021):

▶ “74% of fails in specific issues are effectively “daisy-chain” fails, which could be paired off and hence eliminated with increased central clearing.”

▶ “the percentage of fails that pair off tends to be higher when fails are higher and in issues where they are higher.”

▶ “It follows that expanded central clearing not only reduces the balance sheet resources needed for intermediation overall through reduced settlement fails, but that the benefits are greatest when they are most needed and for the securities for which they are most needed.”