As things stand, swap execution facilities (Sdfs) only exist on paper. But that makes it easier for would-be operators of the platforms to engage in a kind of origami – taking the flat outlines that appear in the Dodd-Frank Act, then folding and bending them to suit changing competitive and strategic dynamics.

Bloomberg is a good example. It plans to launch a cross-asset class Sef that will generate revenues through sales of Bloomberg terminals – but that business model would make it difficult for Bloomberg’s putative Sef to co-operate with a second type of entity that doesn’t yet exist, the Sef aggregator (Risk June 2011, pages 18–22, www.risk.net/2073226).

The idea behind aggregation is that there will be so many first-generation Sdfs in competition that clients will need a service to reunite the market’s fragmented liquidity. Aggregators say they will pay Sdfs they put in their shop window. That doesn’t fit with Bloomberg’s terminal-driven model, but if aggregation is the path the market ends up taking, the model may need a rethink, says Ben Macdonald, the company’s global head of fixed income.

“We’d look at what we’d need to do from a regulatory perspective, and to the extent that we had to be aggregated, we’d look at our business model and make sure we’re comfortable with that. The world is changing; we’d look at our facts and figure out how to operate in this space at that point,” he says.

Aggregators may have to do the same, though. There is no clarity about the regulatory regime that will exist for Sef aggregation, and Macdonald argues the services should be subject to the same kind of rules as Sdfs themselves. “If there’s fragmentation, there will be a market for aggregation. But you need to make sure aggregators don’t become a way to bypass the cost and compliance burden you take on as a Sef. There needs to be equivalence between Sdfs and aggregators to ensure Sdfs aren’t carrying the entire cost of the new regulation, then handing the result of that over to be aggregated – if you end up there, most people will want to be aggregators rather than Sdfs,” he says.

Regarding competition between Sdfs, Macdonald says Bloomberg is in a strong position: “We operate a significant franchise in the fixed-income electronic trading space – around 20,000 people use it on a daily basis globally to execute, through myriad different formats. We don’t operate a one-size-fits-all platform; there are different execution styles depending on the asset class and market,” he says.

The firm currently sees peaks of more than 1,000 trades a day, and its existing ALLQ service aggregates single dealer pages for interest rate and credit default swaps – not a million miles from the service Bloomberg’s Sef will offer. “The difference between ALLQ today and a central limit order book is whether or not names are disclosed, and some other nuances therein – but the basic technology is there. For me, it’s the understanding of which knobs I’m going turn and what settings I’m going to put on the platform to prepare it for the final Sef registration,” he says.

The rule-making process is a little further behind in Europe, but proposals currently include a number of different platform types. It’s not yet clear whether Bloomberg will register as an organised trading facility – a new type of venue proposed as part of the ongoing review of the Markets in Financial Instruments Directive – or as a multilateral trading facility. In the end, Bloomberg could register as one of those, neither of them, or a third category, says Macdonald (Risk May 2012, pages 45–48, www.risk.net/2170964).

“It’s all very theoretical. I would challenge anybody who thinks they have enough information to affirmatively decide what they’re going to register as in Europe,” he says.

“The rules for Sdfs are clearer in the US – it is established, for instance, that dealer platforms cannot be Sdfs. But some politicians are unhappy with the way the proposals have been written, and the Sef Clarification Act now being debated by the US Congress seeks to rein in some of the Commodity Futures Trading Commission’s draft rules, including those requiring quote requests to go to a minimum of five market-makers on a Sef, and a ban on voice trading (Risk May 2012, pages 25–27, www.risk.net/2169518).

Macdonald hopes it succeeds: “It reflects a lot of the feedback that was put into comment letters, including by ourselves. I think there are a lot of dangers with having too prescriptive a set of protocols – you risk ultimately removing liquidity from the system,” he says.

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