PRESS RELEASE

ESMA publishes results of EU central counterparties stress test

The European Securities and Markets Authority (ESMA) has published today the results of its first EU-wide stress test exercise regarding Central Counterparties (CCPs). The exercise is aimed at assessing the resilience and safety of the European CCP sector as well as to identify possible vulnerabilities. The results of the test shows that the system of EU CCPs can overall be assessed as resilient to the stress scenarios used to model extreme but plausible market developments.

ESMA’s stress test solely focused on the counterparty credit risk which CCPs would face as a result of multiple clearing member (CM) defaults and simultaneous market price shocks. Being the first EU-wide stress test exercise for CCPs, ESMA decided to focus on the counterparty credit risk aspects of CCPs and leave additional risk dimensions for future exercises. In addition, ESMA also issued recommendations on how to improve CCPs’ internal methodologies.

ESMA tested the resilience of 17 European CCPs. These CCPs held over €150bn worth of default resources with more than 900 CMs Union-wide. ESMA tested CCPs resources using combinations of CM default and market stress scenarios. The results show that CCPs’ resources were sufficient to cover losses resulting from the default of the top-2 EU-wide CM groups combined with historical and hypothetical market stress scenarios.

However, under more severe stress scenarios, CCPs faced small amounts of total (i.e. across all CCPs) residual uncovered losses varying from 0.1bn up to 4bn Euros. This was especially the case for scenarios assuming the default of the top-2 CMs per CCP due to assumed CM defaults across CCPs. That is a scenario where a CM defaulting in one CCP would also be considered to be in default in all CCPs, in which it is a member, leading to more than 25 CM defaulting EU-wide.
Steven Maijoor, ESMA Chair, said:
“CCPs play a significant role in financial markets by reducing the exposure risk of clearing members. Therefore, ensuring that CCPs are resilient to shocks is an important supervisory tool to mitigate systemic risk. ESMA’s first EU-wide stress test shows that European CCPs are overall well equipped to face the counterparty risk associated with the considered stress scenarios. However, ESMA has also issued recommendations addressed to the National Competent Authorities (NCAs) of CCPs. These recommendations are aimed to ensure on-going resilience which will require follow-up within CCP colleges.”

Clearing member default scenarios
ESMA’s stress test exposed CCPs to three different CM default scenarios, which include:
- *scenario A*: the default of the two CMs with the largest exposures per CCP taking into account the common membership across CCPs;
- *scenario B*: the default of the two groups of CMs EU-wide with the largest aggregate exposures to EU CCPs; and
- *scenario C*: the default of the two groups of CMs EU-wide with the largest aggregate exposures to EU CCPs also weighted by their probability of default.

Market price shock scenarios
Given CM default scenarios alone are in principle not deemed to endanger the resilience of CCPs, extreme market price shocks were also applied to CCPs. These consist of historical and hypothetical scenarios that were subject to defined minimum price shocks and modelled stress scenarios. ESMA’s stress tests also considered the historical and hypothetical scenarios CCPs use on a daily basis to manage their resources – when needed, these scenarios were amended to meet a defined set of minimum shocks covering 36 market risk factors across five asset classes – interest rate, commodity, equity, FX and credit.

Knock-on and reverse stress analysis
The overall exercise was complemented by an inter-dependency analysis of CCPs through their common CMs, including also an assessment of the concentration of CCPs’ exposures and the potential spill-over effects to non-defaulting CMs, triggered by the loss absorption mechanism of CCPs. In addition, a set of reverse stress scenarios was included which further increase the number of defaulting entities in order to look for extreme but plausible stress scenarios that
would significantly impact the resilience of EU CCPs. These reverse stress scenarios have not revealed any plausible scenarios with systemic impact.

**ESMA recommendations**

Although EU CCPs overall seem well equipped to face severe scenarios, ESMA has included recommendations addressed to the NCAs of CCPs. These cover:

- **assessment of the creditworthiness of CMs** – a significant part of CCPs collateral are pooled resources of non-defaulting CMs. In extreme cases, these CM could face significant losses which in turn could trigger the default of further CMs and additional losses at CCP level. Therefore, ESMA recommends that CCPs incorporate in their creditworthiness assessment of CMs, the potential exposures these may face due to their membership in other CCPs. Such analysis is essential in order to identify sources of increased exposure; and

- **methodologies for price shocks** – in the course of data analysis provided by CCPs, ESMA has also identified that in a number of cases the stress price shocks applied by CCPs for some of their cleared products as part of their own stress testing framework are not as conservative as the *minimum shocks* defined for this exercise or do not replicate the most extreme historic price changes observed. To achieve the on-going resilience of CCPs, ESMA recommends NCAs to ensure that CCPs revise their price shocks used in their stress test methodologies where gaps have been identified in the course of the exercise.

The European Market Infrastructure Regulation (EMIR) requires ESMA to conduct EU-wide stress tests of CCPs on an annual basis. The exercise is conducted in cooperation with NCAs, which supervise CCPs through supervisory colleges, and the European Risk Board (ESRB). The stress test used reference data provided by CCPs and NCAs for the end of 2014.

ESMA has also issued a Question and Answers (Q&A) document which explains in more detail the overall scope of the stress tests exercise, the different scenarios and methodologies applied.
Notes for editors

1. **ESMA’s 2015 report on EU-wide CCP stress tests**
2. **Q&As on ESMA’s 2015 report on EU-wide CCP stress tests**
3. **The European Market Infrastructure Regulation (EMIR)**
4. ESMA’s mission is to enhance investor protection and promote stable and orderly financial markets. The mission is based on the three objectives of:
   - investor protection;
   - orderly markets; and
   - financial stability.

   It achieves these objectives through four activities:
   1. assessing risks to investors, markets and financial stability;
   2. completing a single rulebook for EU financial markets;
   3. promoting supervisory convergence; and
   4. directly supervising specific financial entities.

5. ESMA achieves its mission within the European System of Financial Supervision (ESFS) through active cooperation with NCAs and securities markets regulators, in particular the European Banking Authority (EBA) and the European Insurance and Occupational Pensions Authority (EIOPA).

Further information:

**Reemt Seibel**
Senior Communications Officer
Tel: +33 (0)1 58 36 42 72
Mob: +33 6 42 48 29 60
Email: press@esma.europa.eu