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Current trends in the derivatives market

FW discusses current trends in the derivatives market with Jonathan Gilmour, Elinor Samuel, Tom Purkiss and Jamie Errington at Travers Smith.



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FW: How would you describe recent developments in the derivatives market? In what ways are political uncertainty and geopolitical conflict currently influencing market participants?

Errington: The derivatives market is a mature ecosystem. However, it continues to evolve to reflect market trends, geopolitical dynamics and regulatory initiatives. The derivatives market also continues to experience regulatory development, with the most noteworthy recent change within European markets being the European Market Infrastructure Regulation (EMIR 3.0), which came into force in December 2024. This significantly impacts those

entering derivatives transactions with European Union (EU) entities while furthering UK-EU regulatory divergence. The new regulations alter clearing thresholds and reporting requirements, among other things, and introduce new active account requirements to encourage more euro-denominated trades being placed through European-regulated clearinghouses. Recent political uncertainty and geopolitical conflict has certainly affected the derivatives market, creating unpredictable trading conditions forcing market participants to alter their risk management strategies. There is increased appetite for foreign exchange and commodity hedging because of worldwide supply chain

issues, currency volatility and the impact of tariffs. Importantly, global interest rate and inflation increases following the pandemic caused many corporates and asset managers to adopt comprehensive hedging platforms prior to recent geopolitical changes. Accordingly, this turmoil has had less impact than it might otherwise have had.

FW: What regions are experiencing notable growth in derivatives market activity? How great are the opportunities with respect to investment strategies and potential returns in these regions?

Gilmour: Recent data shows that the fastest growing derivatives



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markets are Brazil and India, and the growth is expected to continue, driven in part by the rise in foreign investment in both countries and the increasing number of retail traders participating in these markets. In India, the growth of exchange traded markets is particularly noticeable and, in 2024, India's equity option markets accounted for 89 percent of global trading volumes, according to the Futures Industry Association's recent survey. Brazil is the home of B3, the largest exchange in South America. Brazil's economy has faced many recent challenges, including high inflation, which has limited investment in equities, but strong performance by fixed income assets and an asset management industry with \$1.7 trillion worth of assets under management has fuelled the growth of the Brazilian derivatives market. These are indicative of increasing market activity throughout the emerging economies.

markets. While the interposition of the central counterparty makes the legal relationship between counterparties more complex, it was introduced to mitigate counterparty credit risk and to increase efficiency, by enhancing price transparency and liquidity. More recently, the International Swaps and Derivates Association (ISDA) has developed operational processes to reduce complexity in the market. The ISDA 'common domain model' is a standardised data model that is aimed at automating certain post-trade processes such as data reconciliation. Technological changes will continue to enhance operational efficiency. Blockchain-based distributed ledger technology shows promise as it could allow for greater auditability of transactions across participants in the blockchain. If it were adopted across the industry, it could lead to a reduction in the number of intermediaries and improve operational efficiency.



AI and blockchain technologies are enhancing efficiency, transparency, accessibility and risk management.

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FW: Are you seeing a shift toward standardising operational processes to reduce complexity and increase efficiency in the derivatives market?

Gilmour: The over the counter derivatives market has been increasingly standardised following post-financial crisis regulatory reforms. A requirement for certain interest rate and credit derivatives to be 'cleared' through a central counterparty has been introduced in most developed

FW: In what ways are technological advancements, such as artificial intelligence and blockchain, transforming the derivatives landscape?

Purkiss: Artificial intelligence (AI) and blockchain technologies are enhancing efficiency, transparency, accessibility and risk management, allowing for more innovative and inclusive financial markets. AI algorithms can allow market participants to analyse vast amounts of data,

enhancing decision making and allowing fraudulent activity and anomalies to be identified more effectively. The immutability and decentralised nature of many blockchain technologies also provides for greater security and transparency, and the instantaneous nature of blockchain transactions allows for more efficient real-time settlement. When AI and blockchain technologies are integrated, their combined impact can amplify these benefits. For instance, AI can be used to analyse data and execute trades on blockchain-based platforms, leveraging the security and transparency of blockchain while utilising the advanced analytical capabilities of AI. These advancements are not only reshaping the operational landscape but also driving regulatory changes, influencing market structure and transforming the way participants interact with derivatives products.

FW: How would you characterise regulatory oversight across the derivatives market? What effect are enhanced requirements having on regulated firms' reporting and compliance processes?

Samuel: The derivatives market has been subject to ever increasing regulatory scrutiny since the 2007-09 financial crisis. EMIR, known as 'UK EMIR' in the UK following Brexit, is the primary derivatives regulation in the EU and UK, and was introduced alongside similar regulatory initiatives across

developed economies. EMIR/UK EMIR introduced mandatory transaction reporting, clearing requirements for certain derivatives products and counterparties, and various risk mitigation obligations for uncleared transactions. Many of these requirements are intensifying, most recently seen with the overhaul of the EMIR/UK EMIR reporting regime in 2024 and the changes being introduced under the latest changes to EMIR, known as EMIR 3.0, including the new 'active account' requirement for firms with significant euro-denominated derivatives exposures. Firms engaging in more complex derivatives or securities financing transactions should be mindful that they may be subject to additional regulations, including the Markets in Financial Instruments Directive, the Markets in Financial Instruments Regulation and the Securities Financing Transactions Regulation, in a UK and European context. Accordingly, firms are facing significant compliance and reporting pressures. These regulations require material adjustments to be made by regulated firms in particular, as they are subject to closer inspection by the regulatory bodies. Firms are required to strengthen internal governance functions and allocate sufficient resources for compliance purposes, which often comes at considerable cost.

FW: What trends do you expect to unfold in the derivatives market throughout 2025 and



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Recent data shows that the fastest growing derivatives markets are Brazil and India, and the growth is expected to continue.

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beyond? What factors are set to shape participation and activity levels?

Gilmour: We expect that continuing political and global uncertainty will exert significant influence on the derivatives markets in 2025. Market participants face the challenge of navigating this uncertain landscape and ascertaining what impacts these changes will have on their

businesses and how to mitigate those risks. Naturally, derivatives will play an essential role in hedging strategies and risk management. We expect that political instability and geopolitical conflict and changes to global interest rates will be large drivers of increased derivative use. It remains to be seen how the recent introduction of tariffs will flow through the capital markets, but what is clear is that those changes will have implications

for existing hedging and trading strategies which will need to be recalibrated. Another important factor is technological advancement as innovation will allow a greater range of products to be traded on exchange and in larger volumes, without significant cost increases for the sell-side. ■

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