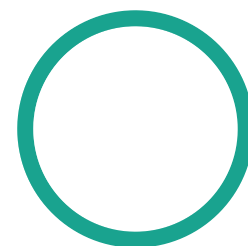
acuiti management intelligence

State of the Market: European Listed Derivatives in 2024

Produced in partnership with:

FIA



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Executive Summary

The last five years have been eventful for the European listed derivatives markets, with market participants having to contend with the outbreak of Covid-19, Russia's invasion of Ukraine, the finalisation of Brexit, and a volatile interest rate environment.

Many of these events have resulted in higher trading volumes as market participants have increased their use of futures and options to hedge their risks or adjust their investment portfolios. But the uplifts in volume were often temporary, and, in some cases, volatility spiked to such high levels that end-users pulled back from the markets and reduced their positions.

At the same time, the pace of regulatory change and technological innovation have not let up, adding to the costs of doing business in Europe and the challenges of keeping up with the competition. The period has also seen the emergence of heightened risks, such as the threat of cyber-attacks, that are putting pressure on firms to increase investment in operational and technological resilience.

Looking ahead, one of the key questions for the industry is how to grow the business while navigating these challenges. In other words, where are the most promising opportunities for growth in the years ahead.

To answer this question, Acuiti partnered with FIA, the leading global association for the exchange-traded derivatives industry, to gauge industry sentiment regarding the key trends, opportunities and challenges facing the industry in Europe.

Acuiti surveyed senior executives at more than 100 firms active in Europe, covering banks (24%), brokers and non-bank FCMs (14%), buyside (20%), principal trading firms (10%), exchanges (16%) and software vendors (15%). 53% of the respondents were based in the European Union, 40% in the UK, and 7% in other parts of Europe.

The survey found that the industry is optimistic about the potential for growth and innovation in Europe, but also aware that other parts of the world may offer better growth prospects.

The survey also found a high level of concern about existing and prospective regulations, as well as the aftereffects of Brexit.

The key findings identified in this report are:

- **Global ambitions:** Many firms see more potential growth in terms of clients and trading volume outside of Europe than inside Europe.
- **Regulatory headwinds**: There is a broad consensus across the market that the alphabet soup of European regulations has created a major burden for the industry.
- **Brexit aftermath**: Most listed derivatives market participants see Brexit as having a negative effect on London's position as a global financial centre and predict that Paris will be the European financial centre with the greatest growth potential over the next five years.
- **Cyber risk**: The threat of disruption from cyber-attacks was identified as the single greatest risk that the industry is currently facing.
- **Growth opportunities**: Futures and options based on interest rates and energy were viewed as having the greatest growth potential over the next five years. Crypto and carbon also look attractive to many firms, although a sizeable number of survey respondents said their firms have no intention of entering these new asset classes.
- **Efficiency vs Innovation**: Views on technology trends vary significantly across the industry. Clearing brokers and other sell-side firms are prioritising gains in efficiency from their investments in technology. In contrast, principal trading firms and exchanges are more interested in innovative new technologies such as artificial intelligence and blockchain.

The path ahead

Growth opportunities

One of the survey questions asked respondents to identify where they see the greatest opportunity for growth over the next five years. As one would expect, many respondents pointed to the potential to grow their business within Europe, but three types of firms saw more potential outside Europe.

Respondents working for sell-side firms, which includes both bank and non-bank brokers, ranked client growth outside Europe as the top opportunity for growth over the next five years. The buy-side, comprising hedge funds and asset managers, expressed the same view.

In addition, respondents working for principal trading firms displayed a similar view — pointing to volume growth in non-European markets as the key growth opportunity for their firms.

The US has been a focus for many firms looking to capitalise on the strengths of its financial markets. For principal trading firms, the huge growth of US retail options trading has created a pull factor. For asset managers and hedge funds, both the out-performance of US single stocks and the centrality of the S&P 500 to global markets have encouraged asset allocation to the region.

This has also been the case in US rates futures markets, by far the deepest and most liquid in the world, which have attracted non-US buy-side and principal trading firms alike.

In addition, many firms have turned to the Middle East and the Asia-Pacific region for growth. For many European sell-side firms, this is a natural evolution of the broadened geographical reach that has been a strong theme of recent years, as volume and client growth in domestic markets has slowed. Existing client demand to trade new geographies has pushed many to establish connectivity to new regional markets — offering access to Chinese, Indian or Brazilian exchanges, for example.

Similarly, buy-side firms are looking to expand their client base and attract new flows from regions outside Europe.

Exchanges, conversely, saw the most upside in European client and volume growth. However, for these respondents, non-European client growth is still a key area of focus. Efforts to capture global trading volumes are already manifest in measures such as the extension of trading hours to increase their appeal in the Asia-Pacific region.

Top opportunities for:

	Sell-side	Buy-side	Prop firms	Exchanges	Software
1	Client growth outside Europe	Client growth outside Europe	Volume growth in non-European markets	Client growth in Europe	Cost reduction and efficiency gains through tech investment
2	Client growth in Europe	Client growth in Europe	Growth of new asset classes	Volume growth in European markets	Client growth outside Europe
3	Cost reduction and efficiency gains through technology investment	Application of new technologies such as artificial intelligence and blockchain/DLT	Application of new technologies such as artificial intelligence and blockchain/DLT	Client growth outside Europe	Application of new technologies such as artificial intelligence and blockchain/DLT
4	Volume growth in non-European markets	Growth of new asset classes	Growth of retail trading	Growth of new asset classes	Growth of new asset classes
5	Growth of new asset classes	Cost reduction and efficiency gains through technology investment	Volume growth in European markets	Growth of retail trading	Client growth in Europe

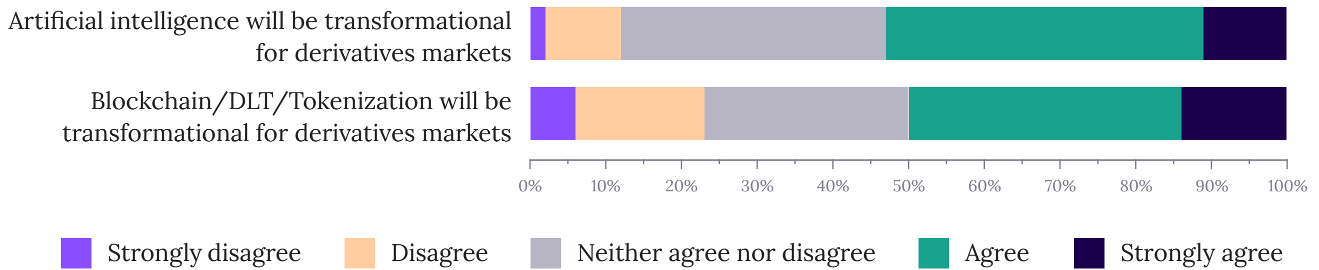
Software vendors also saw opportunity in client growth outside Europe. However, these firms are putting a greater priority on cost reduction and efficiency gains through investment. In part, this reflects the pressures coming from sell-side clients.

Many banks and brokers are pushing to control the costs of their business models as much as possible, either through consolidating the number of outsourced front, middle and back-office systems that they use across their organisations, or through automating trade processes as much as possible.

With the EU's Digital Operational Resilience Act approaching, these sell-side/vendor relationships are set to experience even more pressure to achieve efficiencies (see Section 3).

Technology was given high importance by other firms too, although ambitions for its application varied. For hedge funds, asset managers and principal trading firms, enthusiasm was focused on new technologies, such as artificial intelligence and blockchain/DLT. AI promises significant efficiencies in trading strategies, research, and analysis and in the longer term could also be applied to

Do you agree or disagree with the following statements:

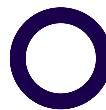


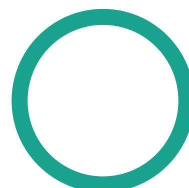
portfolio and collateral management and more widely across operations.

However, this application of the technology is still very much in its infancy. For truly AI-managed firms to take hold as a trend, new models that can go beyond current language models and process the full range of complexities within derivatives trading will have to develop.

With regards to blockchain, efforts to date have been more focused on collateral settlement and optimisation. However, it still early days for DLT adoption, with a clear degree of caution from survey respondents in predicting how transformational it would be for derivatives markets.

While the sell-side has invested in AI and blockchain initiatives, its priorities in technology were cost reduction and efficiency gains, reflecting the cost pressures of their business model. In recent years, this has constituted a close focus on automating as much of the trade processing chain as possible.





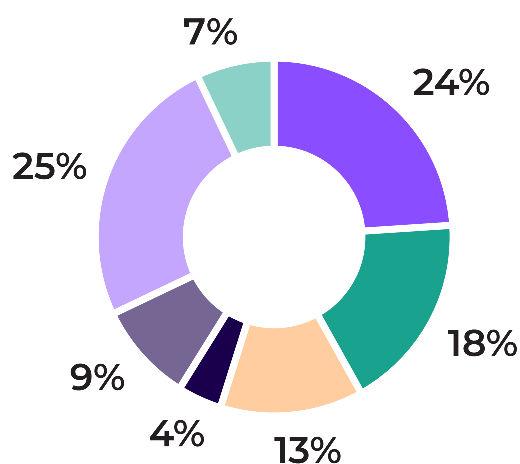
Outlook for trading volumes

When it came to growth opportunities within asset classes, views varied substantially, with cryptocurrency derivatives one example of a market where views were fairly evenly split between enthusiasm and scepticism. Outlooks were fairly divided on interest rates and equities as well, with more enthusiasm overall for the former.

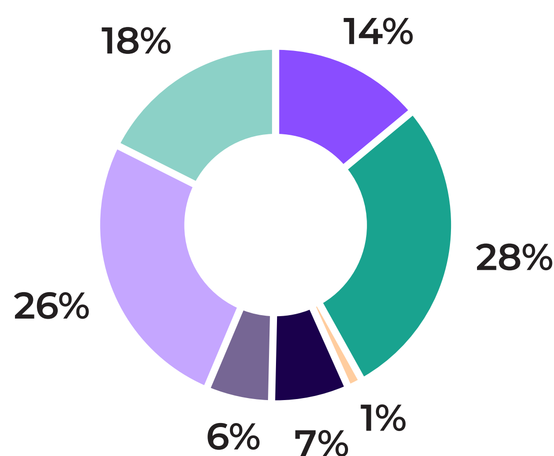
Energy also stood out. Although it was not ranked as highly as other asset classes as having the most potential for higher trading volumes, it had the best ranking in terms of which asset class has the least potential for higher trading volumes. On balance, it had the highest net ranking, which may reflect the fact that the European energy derivatives markets are benefiting from several long-term structural trends.

On the supply side, the pivot away from importing oil and gas from Russia and towards the US is changing how energy producers and merchants use futures and options. On the demand side, the volatility of energy prices has attracted interest from hedge funds.

In which asset class do you see the *most* potential for growth in terms of volumes traded on European listed derivatives markets over the next five years?



In which asset class do you see the *least* potential for growth in terms of volumes traded on European listed derivatives markets over the next five years?



Interest Rates
Equities
Energy
Metals
Commodities
Cryptocurrencies
FX

Sell-side cools on rates growth

Sell-side firms varied substantially in their views on asset class growth — most notably on interest rates, where no bank respondents thought that they offered the most potential in Europe for growth over the next five years as the rates cycle starts to turn negative.

That may reflect a sense among investment banks that the interest rate business has been so strong over the past several years that it cannot grow much more from the current level.

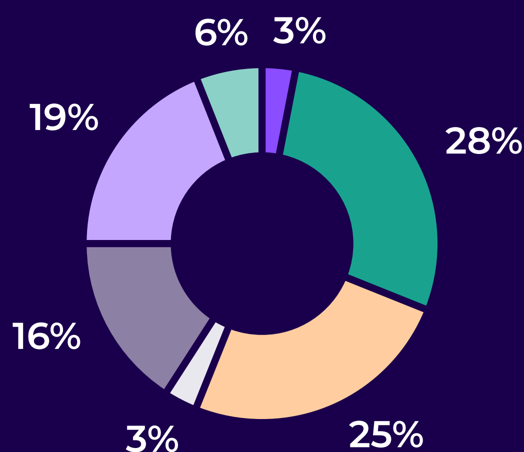
Conversely, futures and options based on equities were viewed most positively, with the most favourable rankings far outweighing the least favourable rankings.

Sell-side firms also were very optimistic about energy derivatives, with higher positive rankings than any other asset class after equities, and no negative rankings at all.

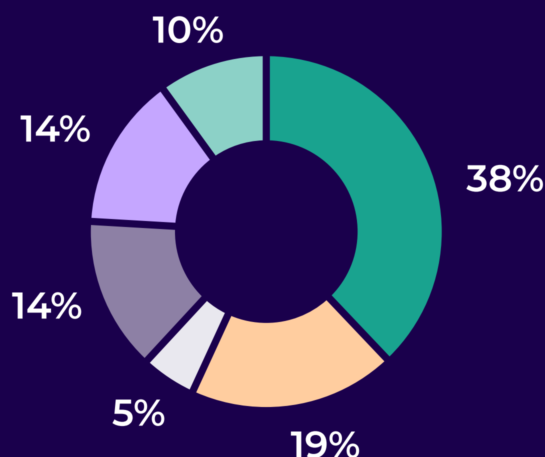
Alongside rates, sell-side firms were bearish on metals and FX. Sell-side firms were most explicitly bearish on cryptocurrency derivatives, again highlighting the continued divisiveness of the asset class (more detail in next subsection).

In which asset class do you see the most potential for growth in terms of volumes traded on European listed derivatives markets over the next five years?

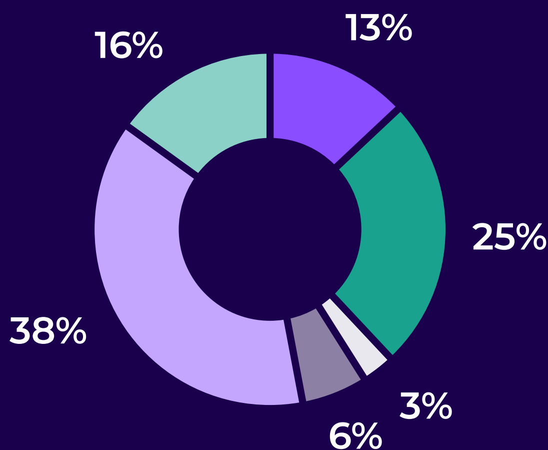
Sell-side overall

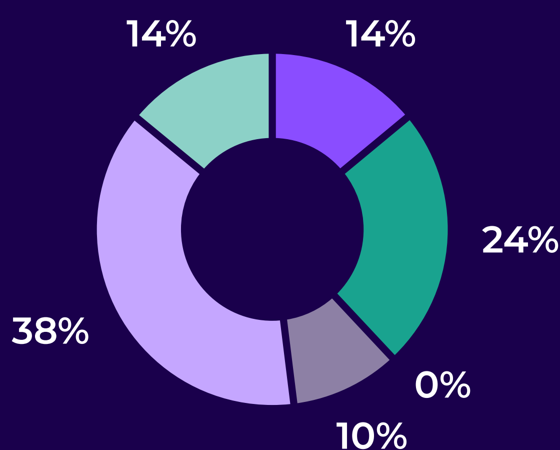


Banks



In which asset class do you see the least potential for growth in terms of volumes traded on European listed derivatives markets over the next five years?





The new asset classes

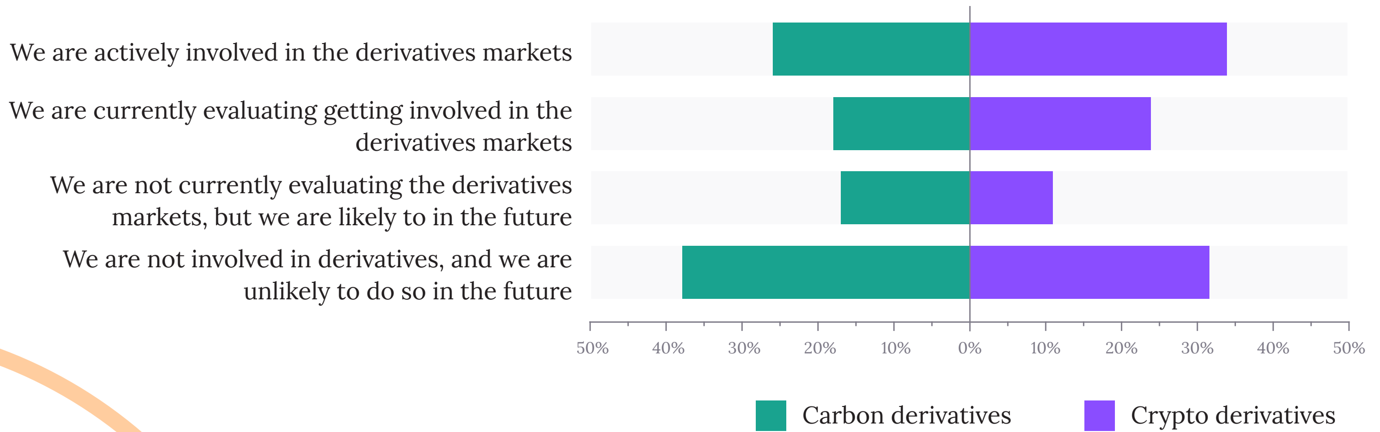
Cryptocurrency and carbon are two spot markets that have generated significant excitement about attendant listed derivatives markets in recent years. Both markets are still nascent compared to the established asset classes, but have also generated track records to be judged on during recent years.

Overall the picture from survey respondents was of cautious adoption of listed derivatives offerings referencing each market. However, enthusiasm was slightly higher for crypto derivatives than carbon.

More than two-thirds of the survey respondents said their firms are either active in crypto derivatives today or planning to engage, whereas slightly less than two-thirds reported that level of involvement and interest in carbon.

Interestingly, crypto adoption rates are being driven by sell-side firms, which have been encouraged by the legal framework provided by the European Union's Markets in Crypto Assets legislation and recent synthesis with traditional finance as new onshore regulated markets

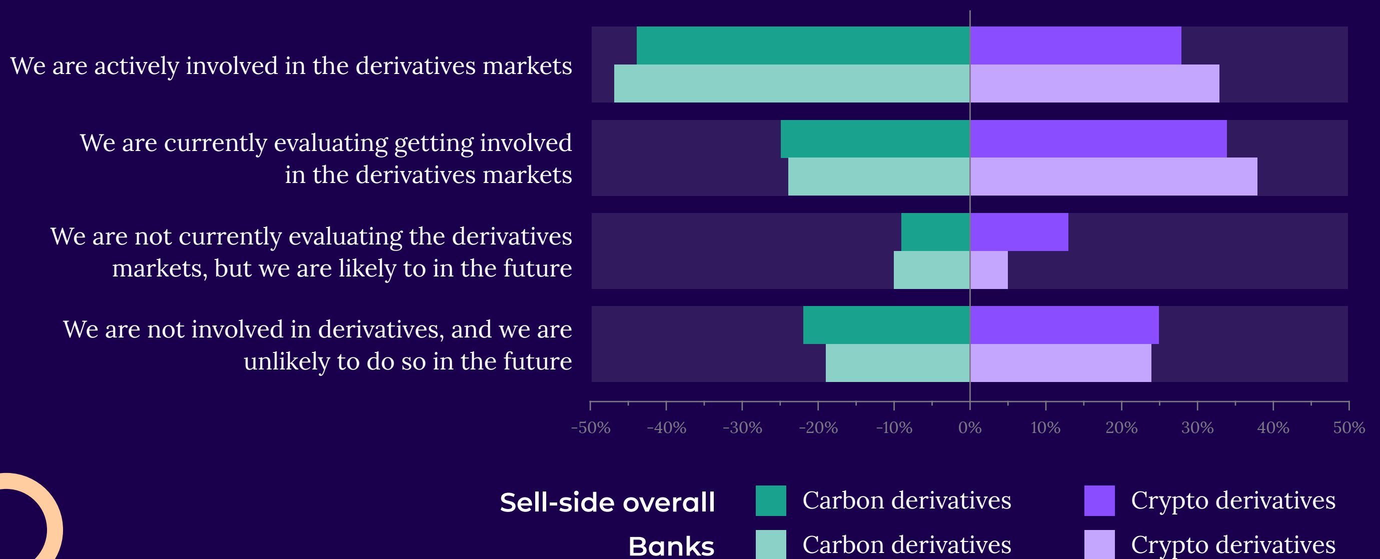
What best describes your company's approach to the trading or offering of derivatives?



Sell-side mobilises on new markets

Sell-side firms, and banks in particular, were more enthusiastic on crypto than the industry overall, as detailed above. They showed even more appetite for carbon, with a high proportion already involved in the market, while a quarter of all sell-side firms and almost the same proportion of banks were preparing to enter the market.

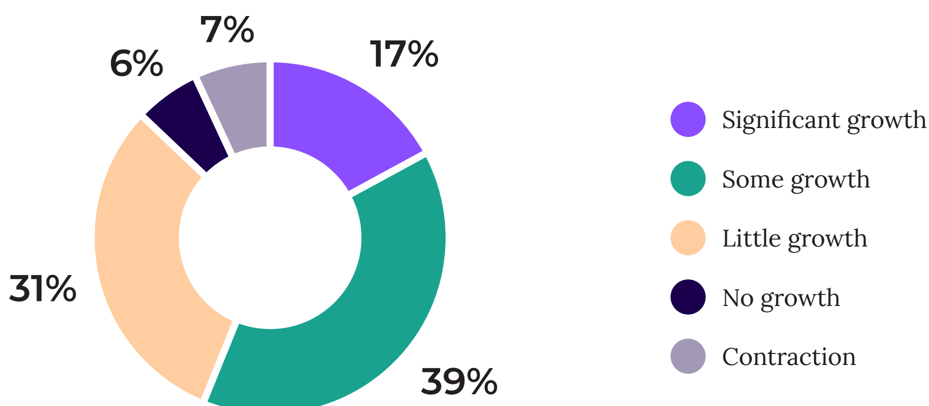
What best describes your company's approach to the trading or offering of derivatives?



Retail

New asset classes have not been the only new source of listed derivatives growth touted in recent years. In light of the impressive growth of retail participation in US options markets, there has been much debate about how similar growth could be achieved in Europe.

Will retail participation in European derivatives markets increase over the next five years?



While most survey respondents predicted growth in retail participation over the next five years, a higher proportion predicted some growth rather than significant growth. Some exchanges and firms are taking active steps to grow retail's participation in listed derivatives, but most recognise it will be a long road to growth and will require significant education. There are also deep structural factors, such as fragmented markets, the popularity of OTC products in Europe and competition from more lightly-regulated jurisdictions for retail flow, that must be contended with.

Challenges to Growth

When considering the top challenges in the five years ahead, 53% of the respondents ranked regulatory burden as the top issue facing their firm. Breaking that down by industry segment, all categories flagged the regulatory burden as the top issue except the sell-side, which put a higher ranking on rising costs.

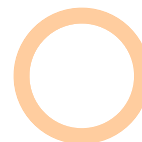
The challenge of rising costs is global. However, there are nuances within European market structure that raises costs further for market participants. The European options market is one example of this, where fragmented market structure has created an expensive trading environment.

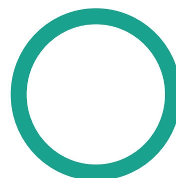
This is an issue for exchanges too, which specifically ranked fragmentation as a key challenge. This has been evident in post-trade areas like clearing, settlement and collateral management (although initiatives are being undertaken to ameliorate these market infrastructure issues at a pan-European level).

The slightly lower ranking of regulation among sell-side institutions reflects how much these firms have had to deal with regulation for the better part of two decades.

While every regulation carries a burden, the compliance teams and expertise that banks have built since the great financial crisis now seem better equipped to decipher and apply new frameworks. In addition, European banks face reduced risks of future increases in capital requirements under Basel III compared with their US peers. This follows last year's statement from the European Banking Authority that only an additional €600m was required across the European banking system to meet Basel III requirements.

For hedge funds and asset managers, low client activity in Europe and declining trading volumes were also major challenges — helping to explain why many are turning their focus to client growth from outside Europe.





Top challenges for:

	Sell-side	Exchanges	Prop firms	Buy-side	Software
C1	Rising costs of doing business	Regulatory burden (excluding capital requirements)	Regulatory burden (excluding capital requirements)	Regulatory burden (excluding capital requirements)	Regulatory burden (excluding capital requirements)
C2	Regulatory burden (excluding capital requirements)	Low client activity in Europe	Capital requirements	Low client activity in Europe	Increased competition from firms in the market today
C3	Capital requirements	Fragmentation of European markets	Declining trading volumes	Declining trading volumes	Low client activity in Europe
C4	Fee compression	Declining trading volumes	Finding skilled staff	Rising costs of doing business	Finding skilled staff
C5	Increased competition from firms in the market today	Rising costs of doing business	Fragmentation of European markets	Competition from new entrants and/ or new business models	Rising costs of doing business

Sell-side firms also ranked fee compression as a key challenge. This was a trend that had broadly lost steam in recent years, with many clients recognising clearing and execution desks' messaging that declining fees and the high upfront costs of competing in these services were squeezing margins too tight.

However, some firms reported that competition for top tier asset manager and hedge fund clients is still a threat to fee structures. For banks trying to compete for business from this limited pool of clients, lowering fees and then trying to renegotiate at a later stage in the relationship is one of few strategies for gaining market share.

Despite these challenges, survey respondents were clearly positive on the future of European listed derivatives markets. Notably, much of the optimism was centred on the intrinsic characteristics of the market, and not new trends. Operational resilience and the ability to innovate from within, rather than any new trend or technology, were recognised as key strengths of the European market today.

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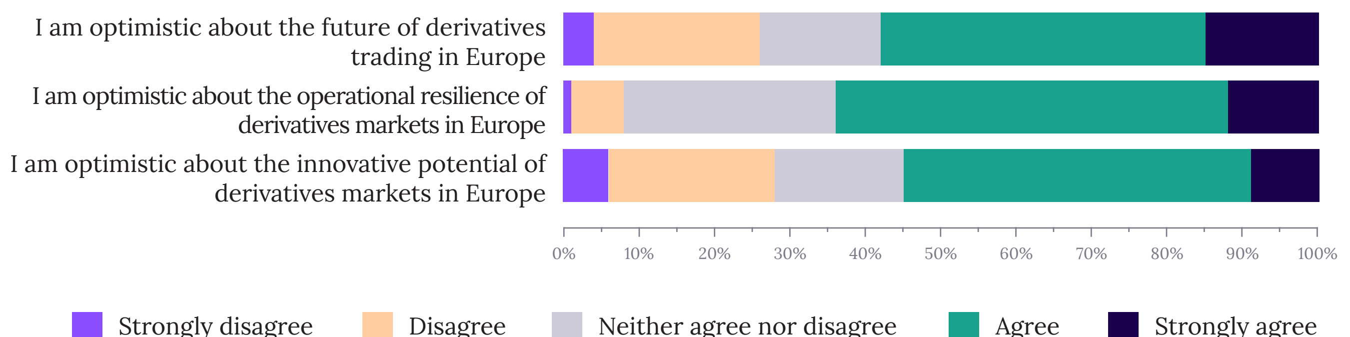

Section 3

Regulation

One of the main challenges identified by all categories of market participants was regulation, which has been a constant of European financial markets since the Global Financial Crisis of 2008.

The new frameworks are lengthy and complex, requiring significant resource mobilisation within firms seeking to navigate the new regulatory environment.

However, it seems that complex regulation is largely now accepted as a fact of life in modern financial markets.

While more survey respondents thought European regulation was disproportionate than proportionate (and many firms still view it as a major challenge, as described in section one) just under a third had no view on the matter.

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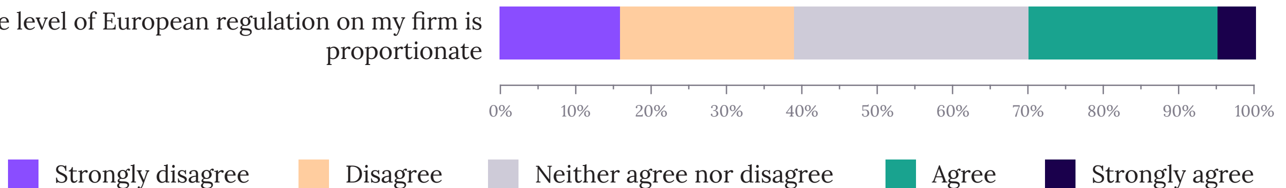


Many also believe that regulation has strengthened the industry.

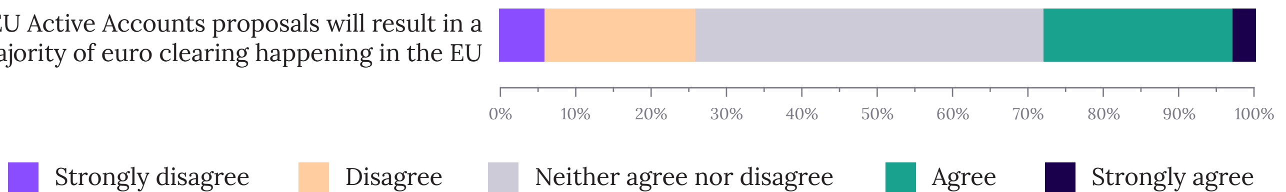
Each of the regulations that market participants were surveyed on carries its unique compliance challenges. How critical market participants rate these challenges in part correlates to how far developed the framework is.

EMIR 3.0 will introduce significant changes to the structure of euro-denominated clearing. It has now been provisionally approved by European co-legislators, with market participants awaiting the final text to be published as well as the issuance of a large number of regulatory technical standards.

In a state of ongoing uncertainty about specifics in several areas, firms will be working to a tight deadline to set up infrastructure such as active accounts and 43% of respondents identified major challenges in implementation.

Active account requirements demand that firms clear a representative number of their trades in certain interest rate derivatives

Do you agree or disagree with the following statement:



contracts through central counterparties in the EU. The measure is the most recent regulatory step to rebalance euro-denominated clearing away from non-EU CCPs. Despite the scale of the ambition, survey respondents showed low conviction on whether the requirements would materially shift the location of euro clearing.

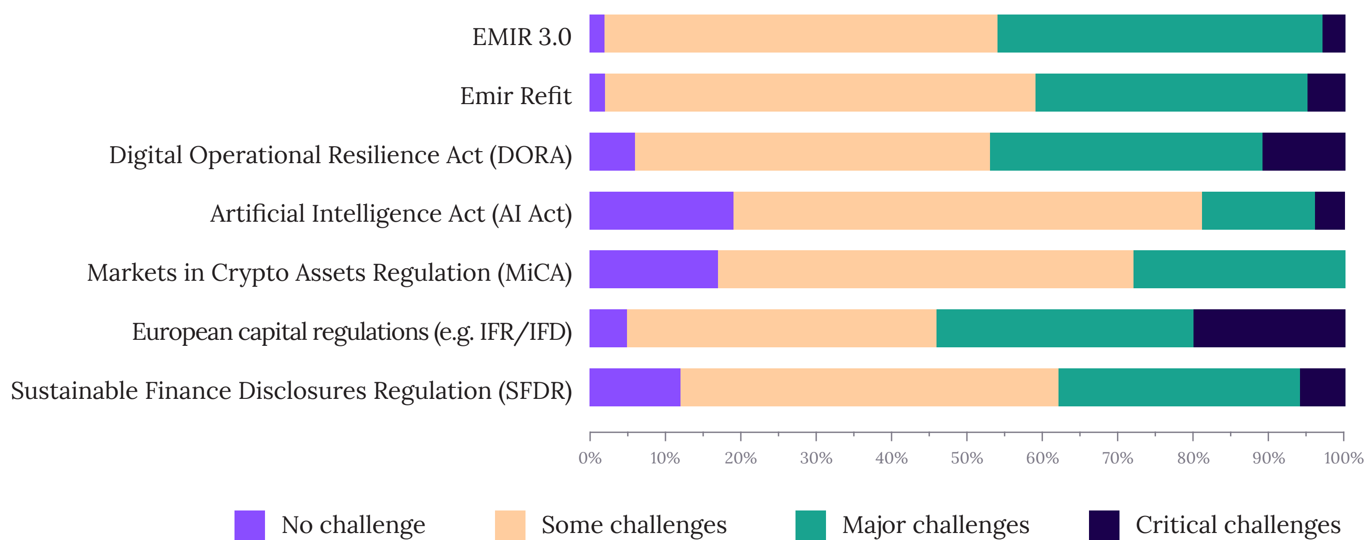
Similarly, the EMIR Refit was an enormous compliance lift for regulatory reporting teams, with many firms having to let its April 29 implementation date pass with some outstanding compliance items. However, it is now established and has diminished somewhat as a challenge.

The EU Digital Operational Resilience Act is also coming into view for firms. The regulation signals a major change in the way that firms interact with their third-party vendors and represents a major operational lift, as reflected in the higher number of firms that foresaw critical challenges in implementing it.

By far the most challenging regulation, however, was IFR/IFD. For principal trading firms, this has constituted a major compliance burden, with significant implications for the prudential requirements that these firms have become subject to under the new EU prudential regime for investment firms.

The cost implications have pushed several principal trading firms to give up their MiFID II licences or relocate their headquarters or certain trading desks outside the EU.

How big a challenge does the implementation of the following EU regulations pose to your firm?



Section 4

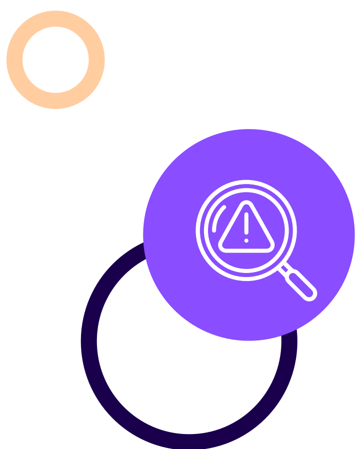
Risks on the horizon

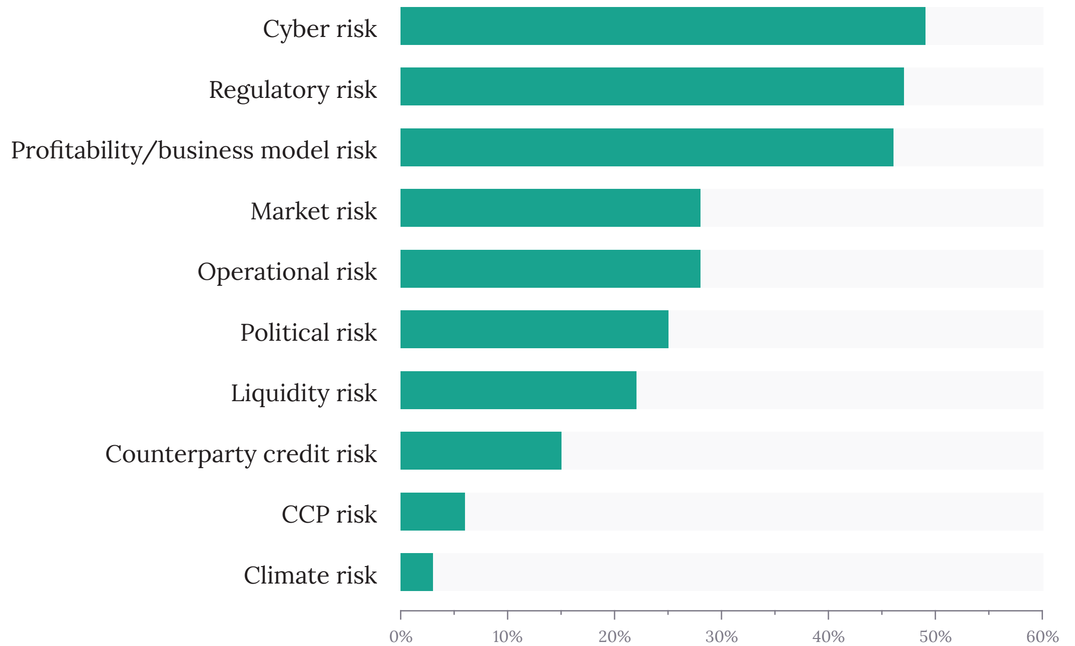
In an increasingly complex world, risk is an inevitable and fast-changing factor for senior executives to understand and mitigate.

Cyber risk is a relatively new threat compared to regulatory and business model risk. The threat of cyber attacks for the clearing industry was brought home last year when ION suffered a ransom-ware attack on its systems. While the issue has subsided in terms of press attention, it is still top of mind for many clearing chiefs and how to improve the resiliency of clearing remains an ongoing discussion.

Since the ION attack, much attention has turned to fallbacks and redundancy systems. In addition, heightened geopolitical tensions have increased the risk of state-sponsored attacks on key financial infrastructure.

Which risks are you most concerned about with regards to your firm today?





These factors explain why market participants ranked cyber risk as their top concern. However, there are two other almost equally pressing concerns in the market today.

Despite the advances that sell-side firms have made with handling the regulatory burden, it remains a substantial load for market participants to deal with.

Regulatory requirements are extensive and require significant engagement with authorities to ensure they are being interpreted correctly.

Regulation is also a constant of listed derivatives markets — when one framework takes effect another is usually coming down the line. While market participants frequently support the objectives of regulation, often there are unexpected consequences from rule proposals. These then require substantial lobbying efforts to counter or moderate.

In extreme cases, regulation can threaten existing business models, as seen with the impact on principal trading firms from IFR/IFD discussed above. This explains why principal trading firms cited regulatory risk as the risk that most concerned them.

Along with cyber risk and profitability/business model risk, regulatory risk was ranked significantly higher than issues like market risk and liquidity risk (although hedge funds and asset managers did rank these two concerns highly too).

There are linkages between the three. A contributing factor to business model risk is the high cost of compliance in listed derivatives markets.

Along with other cost items, such as maintaining and upgrading technological infrastructure and staffing, many firms are battling to maintain margins that are vulnerable to trends like fee compression or low trading volumes.

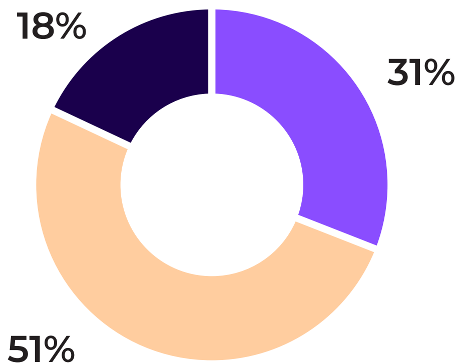
However, the firms most concerned by profitability and business model risk were principal trading firms and software vendors. In the latter case, anxiety may be being driven from greater competition but also DORA, a regulation that encapsulates regulatory and cyber risk.

Brexit

Hovering over many of the challenges that European firms face, especially in the regulatory sphere, is Brexit. Just over four years on from the UK's exit from the EU, and almost a decade since the vote to leave, survey respondents were not upbeat about its consequences or prospects.

While just under a third thought that London would keep its place as a major financial centre with significant growth potential, most foresaw Brexit as causing lasting damage to the City. Should these predictions play out, London's significance as a financial centre will diminish in the coming years.

Which statement best describes the impact of Brexit on London as a financial centre:



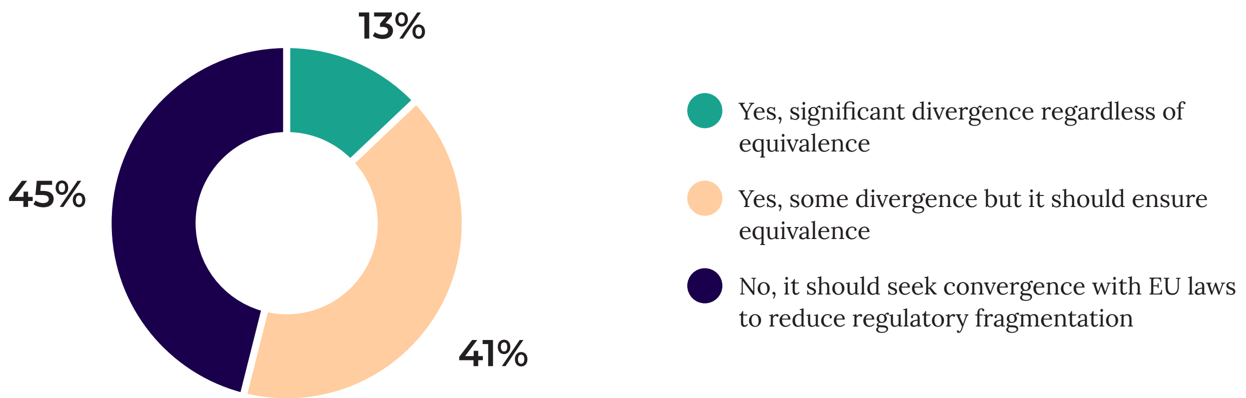
- London will remain a major financial centre with significant growth potential
- London will remain a financial centre but at diminished size and influence
- London will continue to shrink as a financial centre as the EU's capital markets union becomes more established

A key benefit promised within Brexit was the independence to beat a new regulatory path from the EU. However, nearly five years on and what appetite there was for this route has wilted.

While 41% of respondents thought the UK should pursue some divergence from the EU, they did not think this should be done at the expense of equivalence with the bloc's regulations.

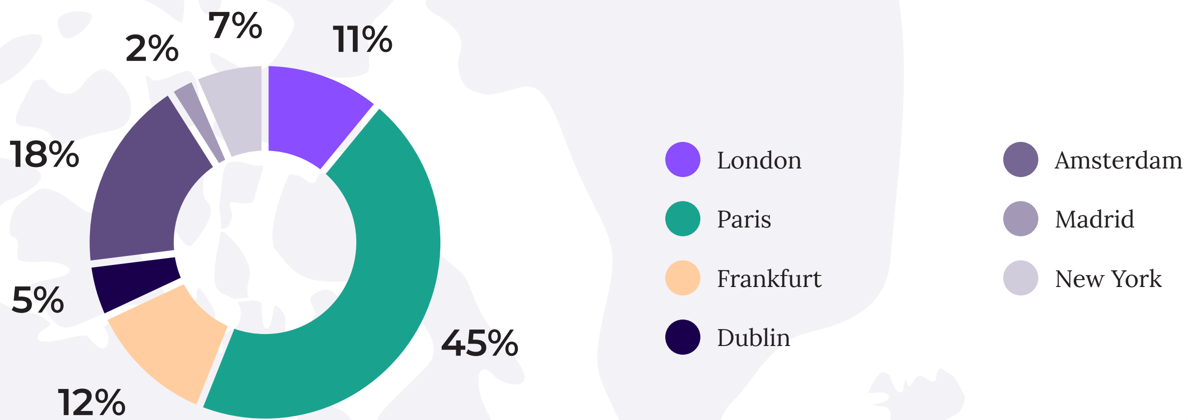
A higher proportion, 45%, thought that the UK should seek convergence as much as possible. For this group, avoiding regulatory fragmentation was the primary objective.

Should the UK diverge from the EU in its rule-making with regards to derivatives?



With their view of Brexit's impact on London a decidedly negative one, survey respondents saw Paris and Amsterdam as the main beneficiaries of the exit in the coming five years. Of the two, Paris was overwhelmingly seen as the city with the most upside.

In the next five years, which city will benefit from Brexit the most in terms of developing as a financial centre?



Conclusion

While the European listed derivatives industry has faced multiple challenges during the last five years, its market participants are viewing the next five years ahead with optimism.

Challenges have not dissipated, with the effects of Brexit still playing out, cyber risk rising as a threat to systems and regulation imposing a constant and heavy burden on operations. However, confronting this multitude of challenges has also created a fortified and resilient industry. There was notable optimism among survey respondents in their ability to withstand shocks and use the foundations that they have created to power innovation in the future.

Despite Europe's lack of growth in terms of listed volumes compared to the US, opportunities abound today as exchanges seek to grow retail participation and new technologies and asset classes continue to evolve in a fast-moving industry.

The key findings identified in this report are:

- **Global ambitions**: Many firms see more potential growth in terms of clients and trading volume outside of Europe than inside Europe.
- **Regulatory headwinds**: There is a broad consensus across the industry that the alphabet soup of European regulations has created a major burden for the industry.
- **Brexit aftermath**: Most listed derivatives market participants see Brexit as having a negative effect on London's stature as a global financial centre and predict that Paris will be the European financial centre with the greatest growth potential over the next five years.
- **Cyber risk**: The threat of disruption from cyber-attack was identified as the single greatest risk that the industry is currently facing.
- **Growth opportunities**: Futures and options based on interest rates and energy were viewed as having the greatest growth potential over the next five years. Crypto and carbon also look attractive to many firms, although a sizeable number of survey respondents said their firms have no intention of entering these new asset classes.
- **Efficiency vs Innovation**: Views on technology trends vary significantly across the industry. Clearing brokers and other sell-side firms are prioritizing gains in efficiency from their investments in technology. In contrast, principal trading firms and exchanges are more interested in innovative new technologies such as artificial intelligence and blockchain.

About the FIA:

FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in Brussels, London, Singapore and Washington, D.C. FIA's membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from about 50 countries as well as technology vendors, law firms and other professional service providers.

FIA's mission is to:
- support open, transparent and competitive markets,
- protect and enhance the integrity of the financial system, and
- promote high standards of professional conduct.

As the principal members of derivatives clearinghouses worldwide, FIA's clearing firm members play a critical role in the reduction of systemic risk in global financial markets.

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